We chose a four-leaf clover as our mark. It's a well-known symbol of good luck and just an all-round interesting shape. And while we've always delivered consistently superior results, strong investment returns, and good fortune to our shareholders, **luck has had very little to do with it.**

2007 ANNUAL REPORT

Celtic
EXPLORATION LTD.

Clover can grow almost anywhere. It's not quite as easy for an oil and gas exploration and production company to grow so effortlessly. **Since 2002, we have created our own good fortune through things like a sound financial platform, quality assets, a disciplined corporate strategy, experienced people and hard work.** In this annual report, we will tell you more about how we nurture every part of our company, so it does what we need it to do – deliver results.

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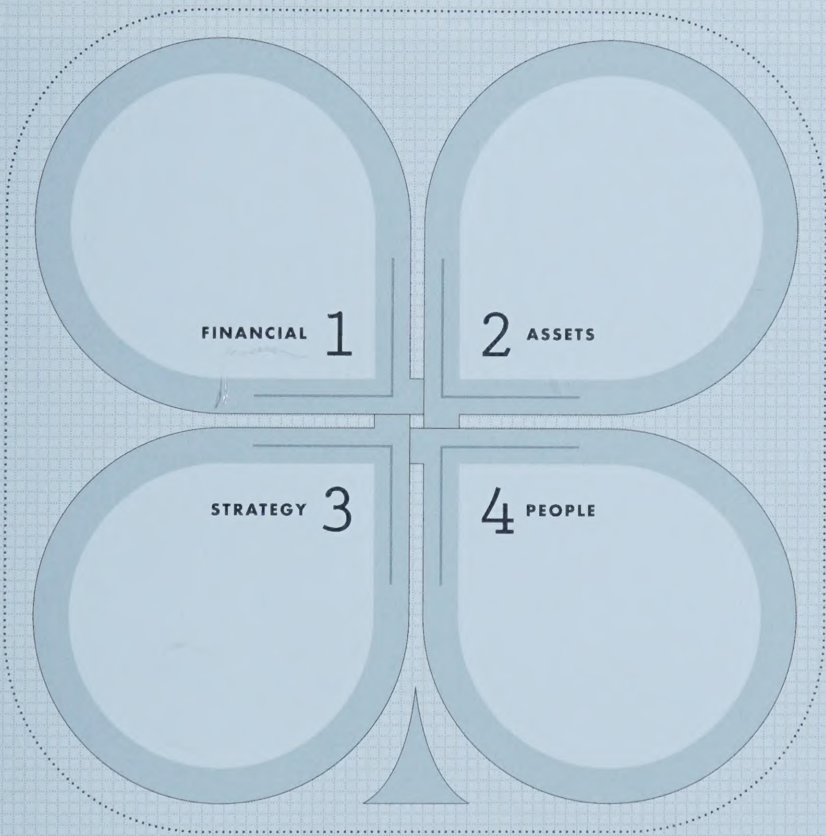
HOW CELTIC KEEPS SHAREHOLDERS IN CLOVER



FINANCIAL PLATFORM
We maintain the financial flexibility to respond quickly to changing market conditions and to capture opportunities as they arise.

QUALITY ASSETS
We have carefully chosen our assets based on strict criteria for sustainable, cost-effective and profitable production.

STRATEGY
Our strategy emphasizes two complementary elements: exploration for quality assets and acquisition of exceptional properties.

PEOPLE
Our managers and staff are among the industry's most experienced, a group keenly focused on creating long-term value for our shareholders.

Commodity markets are notoriously difficult to predict with any certainty. Yet a measure of certainty is exactly what we want to have. When oil and gas prices are unsustainably high, some companies are willing to roll the dice and hope they go even higher. Not us. **We maintain a line of financial defense through a prudent use of hedging.** Our hedging defense has allowed us to maintain cash flow levels that present us with some great opportunities. **No dice. No superstition. No luck.**

FINANCIAL

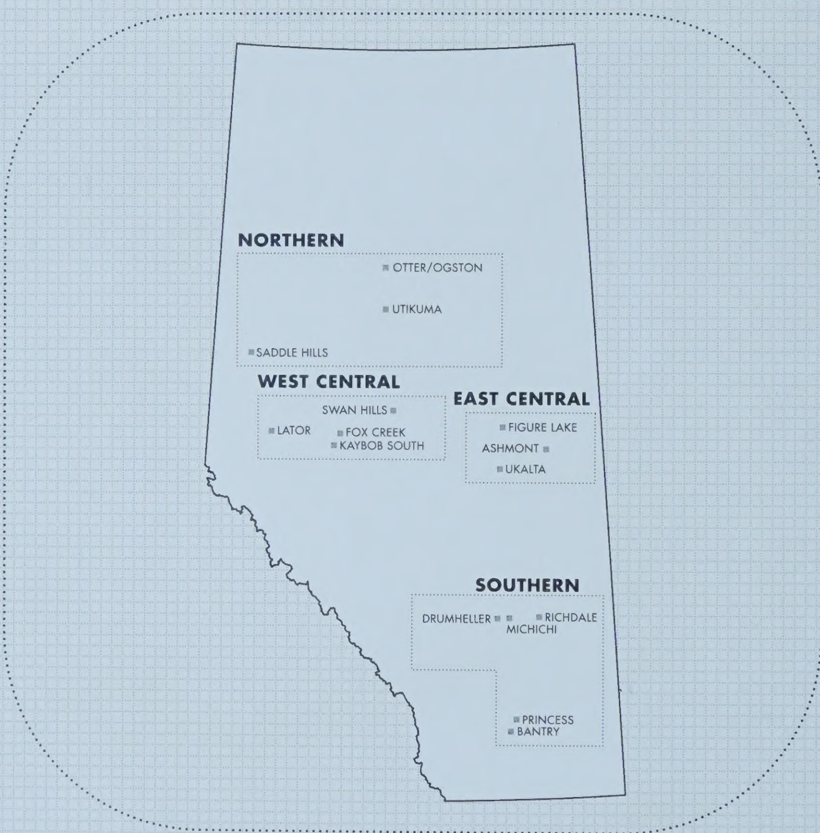
	Three months ended December 31,			Twelve months ended December 31,		
[$ 000s, unless otherwise indicated]	2007	2006	% Change	2007	2006	% Change
Revenue, before royalties and financial derivatives	$ 45,734	$ 31,241	46	$ 151,443	$ 128,344	18
Funds from operations	$ 23,246	$ 19,183	21	$ 83,340	$ 78,541	6
Funds from operations per share						
Basic [$/SHARE]	$ 0.62	$ 0.70	-11	$ 2.34	$ 2.57	-9
Diluted [$/SHARE]	$ 0.61	$ 0.68	-10	$ 2.32	$ 2.50	-7
Net earnings	$ 3,507	$ 6,599	-47	$ 8,198	$ 35,231	-77
Earnings per share						
Basic [$/SHARE]	$ 0.09	$ 0.53	-83	$ 0.23	$ 1.15	-80
Diluted [$/SHARE]	$ 0.09	$ 0.52	-83	$ 0.23	$ 1.12	-79
Capital expenditures, net of dispositions	$ 25,156	$ 32,051	-22	$ 179,789	$ 164,050	10
Total assets				$ 490,431	$ 373,882	31
Bank debt				$ 119,900	$ 101,800	
Working capital deficiency (surplus), excluding bank debt				$ 16,349	$ (3,564)	
Bank debt, net of working capital				$ 136,249	$ 98,236	39
Shareholders' equity				$ 281,463	$ 200,029	41
Common shares outstanding [000s]						
Basic				37,666	32,180	17
Diluted				40,492	34,810	16
Net asset value, discounted at 8% before tax [$/SHARE]				$ 12.99	$ 13.37	-3

OPERATIONS

	Three months ended December 31,			Twelve months ended December 31,		
	2007	2006	% Change	2007	2006	% Change
Production						
Oil [BBLS/D]	3,230	3,290	-2	3,107	3,284	-5
Natural gas [MCF/D]	35,898	18,001	99	28,599	16,072	78
Combined [BOE/D]	9,213	6,290	46	7,873	5,963	32
Production per million shares [BOE/D]	245	196	25	222	195	14
Realized sales prices, after financial derivatives						
Oil [$/BBL]	$ 73.30	$ 58.68	25	$ 68.95	$ 63.78	8
Natural gas [$/MCF]	$ 7.29	$ 10.10	-28	$ 7.76	$ 9.71	-20
Operating netbacks [$/BOE]						
Oil and gas revenue, before hedging	$ 53.55	$ 50.17	7	$ 51.79	$ 54.28	-5
Increased price from physical fixed price contracts	0.41	3.82		0.91	4.69	
Realized gain on financial derivatives	0.17	5.60		2.68	2.29	
Realized sales price, after hedging	$ 54.13	$ 59.59	-9	$ 55.38	$ 61.26	-10
Royalties	(12.31)	(9.67)	27	(11.16)	(10.89)	2
Production expense	(10.57)	(13.38)	-21	(11.11)	(10.90)	2
Transportation and selling expense	(0.81)	(0.75)	8	(0.87)	(0.66)	32
Operating netback	$ 30.44	$ 35.79	-15	$ 32.24	$ 38.81	-17
Drilling activity						
Total wells	8	10	-20	65	83	-22
Working interest wells	8.0	8.4	-5	56.0	62.8	-11
Success rate on working interest wells [%]	100	65	54	81	74	9
Undeveloped land						
Gross acres				327,050	323,821	1
Net acres				248,135	235,308	5
Reserves						
Oil [MBBLS]				11,897	11,634	2
Natural gas [MMCF]				131,253	88,327	49
Combined [MBOE]				33,773	26,355	28
Reserve life index [YEARS]				10.0	11.5	-13

If assets were given out instead of chosen, there might be an element of luck to what you get. But that's not how it works. Companies decide which assets they want to own and how much they're willing to pay. Our strategy has been to use a discipline when it comes to acquiring assets. **We want the best, and our Kaybob South asset is a prime example of getting the best.** Our 50% equity position and ownership of revenue-generating infrastructure puts us in the driver's seat of this high-quality property. It's a good seat to be in.

OPERATING AREAS



NORTHERN

Home to 6% of Celtic's 2007 production, our Northern Alberta assets are consistent with our philosophy of owning higher-quality assets with high netbacks.

EAST CENTRAL

With a further 4% of production here, exclusively natural gas, East Central Alberta holds potential for oil exploration in 2008.

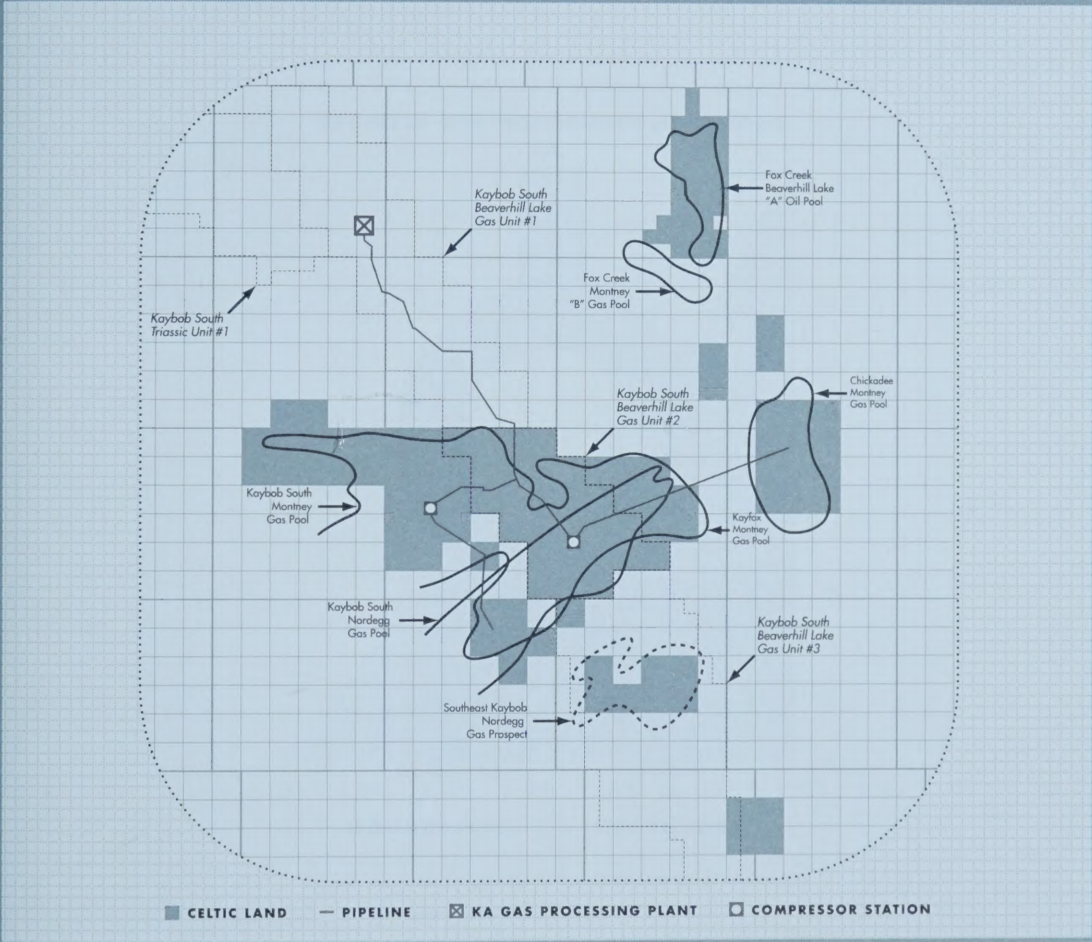
WEST CENTRAL

At 71% of company production, this is clearly where Celtic's present results and future growth opportunities reside.

SOUTHERN

With natural gas properties near Michichi and oil properties near Princess, this area accounts for 19% of Celtic's overall production.

KAYBOB, ALBERTA



Celtic's Kaybob property in West Central Alberta provides a wide range of present and future opportunities in both oil and gas. Celtic owns 76 net sections of land in this area, and maintains control of revenue-generating infrastructure such as compression equipment. A wealth of significant future drilling opportunities are also available, along with the flexibility to move between them to suit market conditions.

For 2008, our capital plans reflect our belief in Kaybob. Kaybob will account for over two-thirds of Celtic's forecasted production and this is where we'll target 75% of our budgeted capital investment.

Some resource companies count on high prices to make their strategy work. But when prices softened in 2007, this oversight was chalked up to either bad strategy or bad luck. We believe there is no better time than now to grow an E&P company. Right now. **Our dual-pronged strategy that we've talked about in past annual reports is more compelling than ever.** But we'll do more than strategize. **We'll continue to use a flexible combination of disciplined exploration and timely acquisitions to meet our long-term goals.** Prices will do what prices do. We'll be prepared one way or the other.

DUAL-PRONG STRATEGY

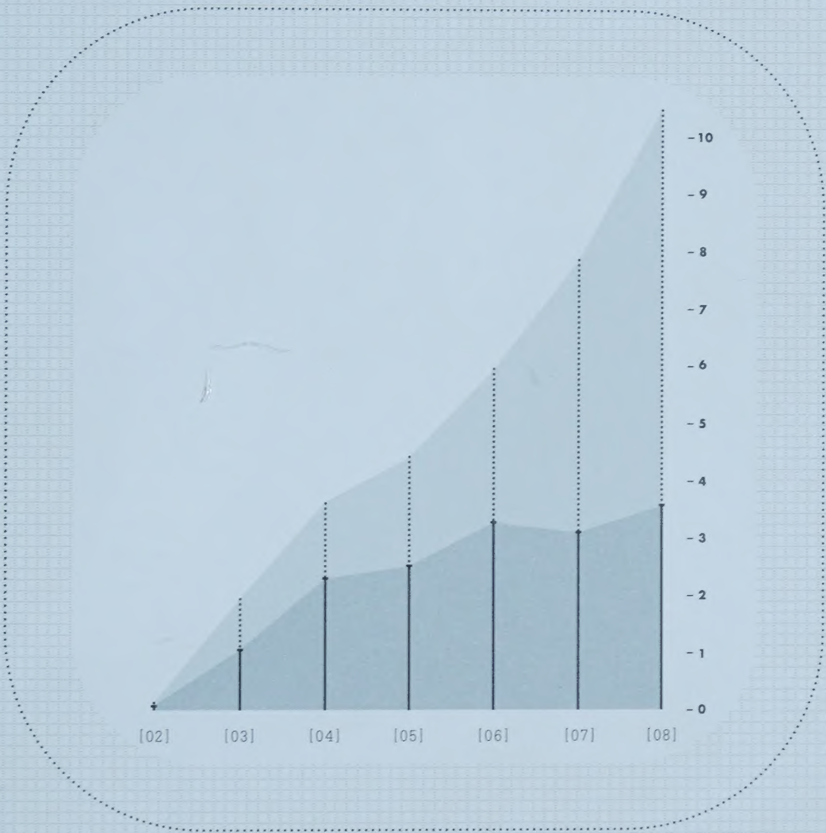
EXPLORATION STRATEGY

Use Celtic's exploration expertise to find high quality assets that fit our production, financial and risk profile.

ACQUISITION STRATEGY

Use Celtic's deal-ready balance sheet to fund opportunistic expansion through the acquisition of quality assets.

OPERATIONS



TOTAL [BOE/D]

[02] 133 [03] 1,941 [04] 3,608 [05] 4,423 [06] 5,963 [07] 7,873 [08] 10,500 PROJECTED

Have we been fortunate? Absolutely. We've attracted and retained a great management team and employee group that is exceptionally talented, passionate and committed. Good people go where they see the greatest opportunity. We get that. That's why we try to be that greatest opportunity. We try to inspire people in all facets of our business. We value people who value the opportunity to make a difference for our shareholders and for the environment. **Our commitment for 2008 is to continue to attract, retain and reward the industry's best professionals to achieve the industry's best performance.** No need to wish us luck.

MANAGEMENT TEAM

[LEFT TO RIGHT]

SADIQ H. LALANI
Vice President, Finance & Chief Financial Officer

DAVID J. WILSON
President & Chief Executive Officer

ALAN G. FRANKS
Vice President, Operations

DAVID C. MORGENSTERN
Vice President, Exploration

MICHAEL R. SHEA
Vice President, Land

Celtic's Annual Meeting of shareholders is scheduled for Wednesday, April 30, 2008 at 3:00 p.m., to be held at The Metropolitan Centre, 333 Fourth Avenue S.W., Calgary, Alberta.

PRESIDENT'S MESSAGE

Celtic Exploration Ltd. ("Celtic" or the "Company") is pleased to report to shareholders on the Company's activities in 2007 Once again, Celtic achieved considerable production and reserves growth in 2007. This occurred during a period which saw industry wide natural gas prices and associated cash flows continue to erode. Celtic was able to maintain its active drilling program during the year with the help of higher priced natural gas financial derivative and fixed price physical contracts. In addition, the Company's production, with a 40% weighting to light oil and liquids, helped enhance the company's cash flow during a period of rising oil prices

Funds from operations of $83.3 million, along with new equity financings totaling $70.8 million (net of costs), contributed towards financing the Company's $179.8 million capital expenditure program in 2007

Along with an active drilling program, Celtic constructed and acquired considerable facility and pipeline infrastructure in its main producing area at Kaybob. Approximately $38.0 million was spent on building infrastructure in 2007 and was augmented with a $45.6 million acquisition in the Kaybob area, which consisted of significant compression facilities and pipelines which were already being used by Celtic. Ownership of these facilities will result in lower operating costs in the Company's main operating area, as Celtic continues to develop the newly discovered Montney natural gas pools over the next several years Celtic currently owns 89 (76 net) sections of land in the Kaybob area of Alberta. The Company has discovered and identified four Montney liquids-rich natural gas pools on these lands, which Celtic commenced acquiring in 2005. To date, only the Kaybob South pool has been down-spaced to three wells per section and development is underway. Initially, the pools are being delineated by drilling one well per section and then during the development stage, horizontal wells are being drilled The horizontal wells are completed using multi-stage fracture technology with five to seven intervals resulting in significantly higher production and reserve recovery rates compared to vertical wells. These wells, at realized natural gas prices of $6 50 per mcf, are expected to payout in less than one year and are forecasted to produce over the next 20 to 30 years

Celtic added 10.3 million BOE of proved plus probable reserves in 2007. This was done at competitive finding, development and acquisition ("FD&A") costs of $19.27 per BOE (including future development capital costs), especially considering the significant amount of land and facility infrastructure expenditures that were included in the FD&A calculation in 2007 With an operating netback of $32.24 per BOE, Celtic achieved a recycle ratio of 1.7 times for 2007 Since inception, the Company's recycle ratio is 2.1 times. Celtic's reserve life index as at December 31, 2007 was 10 0 years and with a large portfolio of development drilling inventory at Kaybob, Celtic will continue to add long-life and high net back reserves over the next several years

With the recent strength in early 2008 in prices for both commodities, Celtic is well positioned with its strong balance sheet and available bank lines to continue an aggressive growth strategy. With an initial capital budget of $120.0 million, the Company is currently in a strong financial position and has the flexibility to either complete an acquisition or increase its development drilling program at Kaybob

We would like to thank our shareholders for their continued support, our Board of Directors for their guidance and our employees for their effort and loyalty. We look forward to continued growth in production and reserves in 2008

DAVID J. WILSON
President and Chief Executive Officer
MARCH 7, 2008

INTRODUCTION

[illegible] ...orated on [illegible] ...pany are listed and posted for trading on [illegible]

[illegible] ...and related notes for the year ended December 31, [illegible] ...tive March 7, 2008. The accompanying financial [illegible] ...ng principles ("GAAP"). [illegible]

Non-GAAP Financial Measurements

This document contains the terms "funds from operations", "operating [illegible] ...ded by operating activities, net earnings or oth[illegible] ...performance calculated in accordance with [illegible] by deducting royalties, production expenses and transportation and [illegible] ...ings per share.

Other Measurements

[illegible] ...otherwise. Where amounts are expressed on a barrel of oil equivalent ("BOE") basis, natural gas volumes have been converted [illegible] ...equivalency conversion method primarily applicable at the burner tip [illegible]

Critical Accounting Estimates

[illegible]

The cost recovery ceiling test is based on estimates of proved [illegible] ...measurement uncertainty and the impact on the fina[illegible] statements could be mat[illegible]

[illegible] ...abandonment and re[illegible]

In order to recognize stock based compensation [illegible] ...may vary ov[illegible]

[illegible] ...reassessment after the lapse of considerable time. Accordingly, the actual income tax liability may differ significantly from that estimated [illegible]

Changes in Accounting Policies and Practices

Details outlining Celtic's accounting policies are contained in the notes to the financial statements

Effective January 1, 2007, the Company has adopted the following new Canadian Institute of Chartered Accountants ("CICA") Handbook sections:

(i) Section 1530, Comprehensive Income,
(ii) Section 3251, Equity,
(iii) Section 3855, Financial Instruments – Recognition and Measurement,
(iv) Section 3865, Hedges, and
(v) Section 1506, Accounting Changes

The standards have been adopted prospectively and therefore, the comparative interim financial statements have not been restated. The adoption of these Handbook sections has no impact on opening retained earnings or opening accumulated other comprehensive income.

Under the revised standards, voluntary changes in accounting polices are permitted only if they result in financial statements which provide more reliable and relevant information. Accounting policy changes are applied retrospectively unless it is impractical to determine the period or cumulative impact of the change. Corrections of prior period errors are applied retrospectively and changes in accounting estimates are applied prospectively by including these changes in earnings. These standards are effective for all changes in accounting policies, changes in accounting estimates and corrections of prior period errors initiated in periods beginning on or after January 1, 2007

Future Changes in Accounting Policies

The following is an overview of CICA accounting standard changes that the Company will be required to adopt in future years

(i) Section 1535, Capital Disclosures,
(ii) Section 3862, Financial Instruments – Disclosures; and
(iii) Section 3863, Financial Instruments - Presentation,

Section 1535 establishes disclosure requirements about an entity's capital and how it is managed. The purpose will be to enable users of the financial statements to evaluate the entity's objectives, policies and processes for managing capital

Sections 3862 and 3863 will replace section 3861, Financial Instruments – Disclosure and Presentation, revising and enhancing its disclosure requirements, and carrying forward unchanged its presentation requirements. These new sections will place increased emphasis on disclosures about the nature and extent of risks arising from financial instruments and how the entity manages those risks

On February 13, 2007, the Accounting Standards Board ("AcSB") confirmed that publicly accountable profit oriented enterprises will be required to use International Financial Reporting Standards ("IFRS") in interim and annual financial statements for fiscal years beginning on or after January 1, 2011. Comparatives must be prepared on the same basis. IFRS will replace Canada's current GAAP for these enterprises. Celtic is currently reviewing the requirements of IFRS and expects to adopt the new standards by the applicable dates

These new standards will be effective for fiscal years beginning on or after October 1, 2007 and the Company will adopt them on January 1, 2008

Disclosure Controls and Procedures

Disclosure controls and procedures are designed to provide reasonable assurances that all relevant information is gathered and reported to senior management, including the Chief Executive Officer ("CEO") and the Chief Financial Officer ("CFO"), on a timely basis in order that appropriate decisions can be made regarding public disclosure. As at December 31, 2007, the CEO and the CFO have evaluated the effectiveness of Celtic's disclosure controls and procedures as defined in Multilateral Instrument 52-109 of the Canadian Securities Administrators and have concluded that such disclosure controls and procedures are effective

Internal Controls over Financial Reporting

The CEO and CFO are responsible for designing internal controls over financial reporting or causing them to be designed under their supervision in order to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with Canadian GAAP. As at December 31, 2007, management, including the CEO and the CFO, has designed Celtic's internal controls over financial reporting as required by Multilateral Instrument 52-109 of the Canadian Securities Administrators

During the review of the design of internal controls over financial reporting for the year ended December 31, 2007, it was noted that, due to the limited number of staff at Celtic, it is not feasible to achieve complete segregation of incompatible duties. However, other internal controls over financial reporting have been designed which provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements

Due to its inherent limitations, internal controls over financial reporting may not prevent or detect misstatements. In addition, projections of any evaluation relating to the effectiveness in future periods are subject to the risk that controls may become inadequate as a result of changes in conditions, or that the degree of compliance with policies and procedures may deteriorate

GROWTH STRATEGY

Celtic growth strategy is dual-pronged. The Company seeks to acquire assets with exploitation potential and, at the same time, implements its full cycle exploration and development program. This strategy has proved successful to date as is evidenced by Celtic's rapid growth since commencing active oil and gas operations in September 2002. To complement this strategy, the Company has assembled a team of experienced and qualified personnel and is well positioned financially to act quickly on new opportunities. Celtic believes that its growth strategy will continue to increase funds from operations per share, net asset value per share and production per share.

RESULTS OF OPERATIONS

2007 HIGHLIGHTS The year ended December 31, 2007 was another successful year in the execution of the Company's growth strategy. Highlights for 2007 are as follows:

- Accumulated 89 (76 net) sections of land in the greater Kaybob area where the Company has made liquids-rich natural gas new pool discoveries in the Montney and Nordegg formations,
- Generated gross proceeds of $70.9 million by completing an equity financing that resulted in the issuance of 3.2 million common shares at a price of $14.35 per share and a flow through share private placement that resulted in the issuance of 1.5 million common shares at a price of $16.65 per share;
- Drilled 65 (56.0 net working interest) wells during the year resulting in 7 (5.7 net) oil wells, 38 (37.3 net) natural gas wells and 8 (2.6 net) coal bed methane wells, for an overall success rate, based on net wells, of 81%;
- Reported earnings per share, diluted, of $0.23, compared to $1.12 per share in 2006;
- Reported funds from operations per share, diluted, of $2.32, a decrease of 7% from $2.50 per share in the previous year;
- Generated an average operating netback of $32.24 per BOE, down 17% from $38.81 per BOE in 2006;
- Increased average daily production by 32% to 7,873 BOE per day, up from 5,963 BOE per day in 2006 and achieved daily average production per million shares of 222 BOE per day, up 14% in 2007 compared to 195 BOE per day in the previous year;
- Increased proved plus probable reserves by 28% to 33.7 million BOE, up from 26.4 million BOE at December 31, 2006 and increased net undeveloped land holdings by 5% to 248,135 acres compared to 235,308 acres at December 31, 2006; and
- Reported a net asset value per share at year-end of $12.99, based on net present value of reserves discounted at 8%, before tax and $11.80 per share using a 10% discount rate, before tax.

PRODUCTION Oil and gas production in 2007 increased 32% to average 7,873 BOE per day compared to 5,963 BOE per day in 2006. Average production in the fourth quarter of 2007 was 9,213 BOE per day. Production per million shares outstanding in 2007 averaged 222 BOE per day, up 14% from 195 BOE per day in 2006. The following table provides a summary of daily average production for the past three years:

PRODUCTION SUMMARY

Year ended December 31,	2007	2006	2005
Oil [BBLS/D]	3,107	3,284	2,524
Natural gas [MCF/D]	28,599	16,072	11,396
Combined [BOE/D]	**7,873**	**5,963**	**4,423**
Production per million shares [BOE/D]	**222**	**195**	**159**

Celtic's production is entirely based in Alberta and is divided into four core areas. In Southern Alberta, the Company's primary natural gas producing properties are located at Drumheller, Michichi and Richdale and its primary oil producing properties are located at Princess and Bantry. In East Central Alberta, the principal producing asset is a shallow natural gas property at

Ashmont and Figure Lake. In Northern Alberta, the Company produces mainly light oil from Ogston, Otter and Utikuma Lake. In West Central Alberta, Celtic has both natural gas and light oil production at Kaybob South, Fox Creek and Swan Hills. West Central Alberta will be the Company's most active drilling area in 2008. In 2007, approximately 70% of Celtic's production came from this area. The following table provides a summary of daily average production in each core area:

PRINCIPAL PRODUCING PROPERTIES [BOE/D]

Year ended December 31,	2007	2006	2005
West Central Alberta	5,498	3,049	1,530
Southern Alberta	1,503	1,838	1,865
Northern Alberta	438	605	638
East Central Alberta	434	471	390
Total	**7,873**	**5,963**	**4,423**

REVENUE Revenue, before royalties, and before realized and unrealized gains or losses on financial derivatives, for the year ended December 31, 2007 was $151.4 million, an increase of 18% compared to $128.3 million in the previous year. For the three months ended December 31, 2007, revenue was $45.7 million, up 46% from $31.2 million in the fourth quarter of 2006. The breakdown of revenue for the past three years is summarized in the following table:

REVENUE

Year ended December 31,	2007		2006		2005	
	[$ 000s]	[$/BOE]	[$ 000s]	[$/BOE]	[$ 000s]	[$/BOE]
Oil revenue	78,267	69.02	78,421	65.43	57,176	62.06
Natural gas revenue	73,176	42.06	49,923	51.12	40,031	57.78
Royalties	(32,062)	(11.16)	(23,710)	(10.89)	(17,730)	(10.98)
Realized gain (loss) on financial derivatives	7,702	2.68	4,993	2.29	(2,899)	(1.80)
Unrealized gain (loss) on financial derivatives	(12,711)	(4.42)	13,635	6.27	-	-
Revenue	**114,372**	**39.80**	**123,262**	**56.64**	**76,578**	**47.43**

The combined average product price received for oil and gas sales, adjusted for realized gains or losses on financial derivatives for the year ended December 31, 2007 was $55.38 per BOE, a decrease of 10% compared to the previous year. For the three months ended December 31, 2007, the average adjusted product price received was $54.13 per BOE, down 9% from the average adjusted price received in the fourth quarter of 2006.

OIL OPERATIONS Oil production for the year ended December 31, 2007 averaged 3,107 bbls per day a decrease of 5% compared to the previous year. For the three months ended December 31, 2007, average oil production was 3,230 bbls per day, down 2% from the fourth quarter of 2006.

The average price received for oil sales, after realized financial derivatives, for the year ended December 31, 2007 was $68.95 per bbl, an increase of 8% compared to the previous year. For the three months ended December 31, 2007, the average oil price received was $73.30 per bbl, up 25% from the average price received in the fourth quarter of 2006.

For the year ended December 31, 2007, average oil royalties were 22.5% of sales, after financial derivatives (22.4% of sales, before financial derivatives). In the previous year, average oil royalties were 21.0% of sales, after financial derivatives (20.5% of sales, before financial derivatives).

Transportation and selling expenses for oil production in 2007 averaged $0.71 per bbl compared to $0.54 per bbl in 2006. The higher per unit cost in 2007 reflects the larger percentage of oil production that was trucked in contrast to the previous year.

For the year ended December 31, 2007, production expenses were $13.99 per bbl. In the previous year, production expenses were $12.30 per bbl. The higher per unit production expense in 2007 reflects the higher costs incurred to operate oil handling facilities.

The breakdown of oil netbacks is summarized in the following table:

OIL NETBACK

Year ended December 31,	2007		2006		2005	
	[BBLS/D]	[$/BBL]	[BBLS/D]	[$/BBL]	[BBLS/D]	[$/BBL]
Daily average production	**3,107**		**3,284**		**2,524**	
Sales price		69.02		65.43		62.06
Gain (loss) on financial derivatives		(0.07)		(1.65)		(3.15)
Royalties		(15.49)		(13.40)		(10.58)
Production expense		(13.99)		(12.30)		(10.93)
Transportation and selling expense		(0.71)		(0.54)		(0.61)
Oil netback		**38.76**		**37.54**		**36.79**

NATURAL GAS OPERATIONS Natural gas production for the year ended December 31, 2007 averaged 28,599 mcf per day, an increase of 78% compared to the previous year. For the three months ended December 31, 2007, average natural gas production was 35,898 mcf per day, up 99% from the fourth quarter of 2007. Increases in natural gas production in 2007 were primarily a result of Celtic's successful drilling results at Kaybob South, Alberta.

The average price received for natural gas sales, after realized financial derivatives, for the year ended December 31, 2007 was $7.76 per mcf, a decrease of 20% compared to the previous year. For the three months ended December 31, 2007, the average natural gas price received was $7.29 per mcf, down 28% from the average price received in the fourth quarter of 2006.

For the year ended December 31, 2007, average natural gas royalties were 17.9% of sales, after financial derivatives (19.8% of sales, before financial derivatives). In the previous year, average natural gas royalties were 13.4% of sales, after financial derivatives (15.3% of sales, before financial derivatives). Lower royalty rates in 2006 were primarily a result of significant increases in revenue resulting from physical fixed price contracts and realized gains on financial derivatives. Actual royalties payable are based on an Alberta reference price and not on actual corporate realized prices. In addition, higher royalty rates in 2007 reflect the expiration of certain royalty holiday wells during the year and the acquisition of certain higher royalty rate wells that were completed in 2007.

Transportation and selling expenses for the year ended December 31, 2007 were $0.16 per mcf, an increase of 23% compared to $0.13 per mcf for the previous year. With a 78% increase in natural gas production in 2007 over the previous year, per unit transportation costs were higher in 2007 as a result of the higher per unit costs relating to the increased production.

For the year ended December 31, 2007, production expenses were relatively unchanged from the previous year. In 2007 production expenses were $1.54 per mcf compared to $1.53 per mcf in the previous year.

The breakdown of natural gas netbacks is summarized in the table on the following page.

NATURAL GAS NETBACK

Year ended December 31,	2007		2006		2005	
	[MCF/D]	[$/MCF]	[MCF/D]	[$/MCF]	[MCF/D]	[$/MCF]
Daily average production	**28,599**		**16,072**		**11,396**	
Sales price		7.01		8.52		9.63
Gain on financial derivatives		0.75		1.19		-
Royalties		(1.39)		(1.30)		(1.92)
Production expense		(1.54)		(1.53)		(1.27)
Transportation and selling expense		(0.16)		(0.13)		(0.15)
Natural gas netback		**4.67**		**6.75**		**6.29**

FUTURE CHANGES TO ROYALTIES On October 25, 2007, the Government of Alberta released a report entitled "The New Royalty Framework" ("NRF") whereby Crown royalty rates will change effective January 1, 2009. Included in the NRF is a lower royalty rate incentive for deep natural gas wells which Celtic is assuming will apply to qualifying wells, regardless of when they were drilled.

The Company has not used the new proposed royalty rates in its December 31, 2007 independent reserves evaluation, as these changes had not been enacted into law as at December 31, 2007. However, Celtic has prepared an internal re-run of its December 31, 2007 reserves evaluation using the new royalty rates proposed in NRF, without changing the forecasted commodity prices in the evaluation. The results indicate that royalties' payable in 2009 would increase by 5.6% and therefore, negatively affect estimated 2009 cash flow by 2.6%. However, the net present value of reserves, using a 10% discount rate, before tax, and proved plus probable reserves, would increase by 2.0%.

The government is currently reviewing certain possible unintended consequences of NRF and Celtic expects further clarification from the government soon. The Company has been pro-active during the process and has provided the government with documentation that Celtic believes highlights possible unintended consequences that require further attention.

INTEREST EXPENSE The Company has a committed term credit facility. The authorized borrowing amount under this facility is $165.0 million. Interest is payable monthly for borrowings through direct advances. Under the credit facility, borrowings through the use of bankers' acceptances are also available. Security is provided for by a floating charge debenture over all assets in the amount of $250.0 million, general assignment of book debts and a fixed charge on the Company's major producing petroleum and natural gas properties Repayments of principal are not required provided that the borrowings under the facility do not exceed the authorized borrowing amount and the Company is in compliance with all covenants, representations and warranties. The credit facility revolves until May 3, 2008, at which time the financial institutions will complete their annual review.

Interest expense for the year was $6.3 million at an average rate of 5.8% compared to $4.0 million at an average rate of 5.6% in 2006.

INTEREST EXPENSE

Year ended December 31,	2007		2006		2005	
	[$ 000s]	[$/BOE]	[$ 000s]	[$/BOE]	[$ 000s]	[$/BOE]
Interest expense	6,268	2.18	3,959	1.82	1,079	0.67
Average debt outstanding	107,559		71,129		25,666	
Average interest rate [%]	**5.8**		**5.6**		**4.2**	

GENERAL AND ADMINISTRATIVE EXPENSES General and administrative expenses for the year ended December 31, 2007 were $3.0 million or $1.06 per BOE compared to $2.0 million or $0.91 per BOE in 2006. General and administrative expenses are reduced by overhead recovered on Company operated properties. In addition, salaries relating to geological and geophysical personnel are capitalized. The following table provides a breakdown of general and administrative expenses:

GENERAL AND ADMINISTRATIVE EXPENSES

Year ended December 31,	2007		2006		2005	
	[$ 000s]	[$/BOE]	[$ 000s]	[$/BOE]	[$ 000s]	[$/BOE]
Gross general and administrative expenses	6,315	2.20	5,505	2.53	4,707	2.92
Overhead recoveries	(2,781)	(0.97)	(2,989)	(1.37)	(2,339)	(1.45)
Capitalized overhead	(501)	(0.17)	(539)	(0.25)	(459)	(0.28)
General and administrative expenses	**3,033**	**1.06**	**1,977**	**0.91**	**1,909**	**1.19**

EMPLOYEES

At December 31,	2007	2006	2005
Head office	33	31	29
Field operations	10	8	6
Total Employees	43	39	35

STOCK BASED COMPENSATION EXPENSE For the year ended December 31, 2007, stock based compensation expense was $1.5 million, compared to $1.1 million in 2006. The fair value of each option granted is estimated on the date of grant using the Black-Scholes option pricing model with weighted average assumptions shown in the following table:

STOCK BASED COMPENSATION EXPENSE

Year ended December 31,	2007		2006		2005	
	[$ 000s]	[$/BOE]	[$ 000s]	[$/BOE]	[$ 000s]	[$/BOE]
Stock based compensation expense	**1,453**	**0.51**	**1,121**	**0.52**	**844**	**0.52**
Weighted average assumptions for stock options granted:						
Risk-free interest rate [%]	4.50		4.25		4.00	
Expected life in years	3.0		3.0		3.0	
Expected volatility [%]	20		20		22	
Expected dividend yield [%]	-		-		-	

DEPLETION, DEPRECIATION AND AMORTIZATION The Company follows the full cost method of accounting whereby all costs relating to the exploration and development of oil and gas reserves are capitalized. These capitalized costs along with estimated future capital expenditures to be incurred in order to develop proved reserves, are depleted and depreciated on a unit of production basis using estimated proved oil and gas reserves. Depreciation of furniture and office equipment is provided using the declining balance method at a rate of 25%. Estimated future costs relating to asset retirement obligations are provided for on a unit of production basis, and the provision is included in depletion, depreciation and amortization.

Depletion, depreciation and amortization expense for the period ended December 31, 2007 was $63.2 million or $21.98 per BOE, compared to the previous year's amount of $43.4 million or $19.96 per BOE.

The following table provides a summary of the amounts included in depletion, depreciation and amortization:

DEPLETION, DEPRECIATION AND AMORTIZATION

Year ended December 31,	2007		2006		2005	
	[$ 000s]	[$/BOE]	[$ 000s]	[$/BOE]	[$ 000s]	[$/BOE]
Depletion - intangible P&NG assets	47,198	16.42	33,039	15.19	21,955	13.61
Depreciation - tangible P&NG assets	15,311	5.33	9,772	4.49	6,374	3.95
Depreciation - other assets	155	0.05	119	0.05	100	0.06
Amortization - asset retirement costs	513	0.18	503	0.23	434	0.27
Depletion, depreciation and amortization	**63,177**	**21.98**	**43,433**	**19.96**	**28,863**	**17.89**

CEILING TEST The Company performed a ceiling test calculation at December 31, 2007 in accordance with the CICA full cost accounting guidelines. As a result of the calculation, Celtic was not required to record an impairment loss. In addition, based on the calculation in the previous year conducted at December 31, 2006, there was no impairment loss required. The forecasted future oil and gas prices for the next five years used in the ceiling test evaluation of the Company's proved reserves as at December 31, 2007 are included in the notes to the financial statements.

TAXES For the year ended December 31, 2007, Celtic provided for a recovery of future income taxes in the amount of $2.5 million. This amount differs from the expected provision for income taxes of $1.8 million based on the statutory combined income tax rate of 32.1% due to the differences between non-deductible stock based compensation costs and the recognition of a benefit of $4.8 million primarily relating to substantively enacted changes to future federal income tax rates. An analysis of the income tax provision is included in the notes to the financial statements.

At December 31, 2007, Celtic had unused income tax deductions available of approximately $304.5 million. A summary of these deductions with corresponding rates of deductibility is shown in the table below:

INCOME TAX DEDUCTIONS

Year ended December 31,	2007		2006		2005	
	[$ 000s]	DEDUCTION RATE [%]	[$ 000s]	DEDUCTION RATE [%]	[$ 000s]	DEDUCTION RATE [%]
Canadian oil and gas property expense [COGPE]	69,500	10	39,382	10	30,692	10
Canadian development expense [CDE]	93,500	30	70,999	30	47,017	30
Canadian exploration expense [CEE]	42,800	100	43,153	100	22,862	100
Undepreciated capital cost [UCC]	94,000	4 to 30	67,508	4 to 30	39,568	4 to 30
Share issue costs	4,700	5 YEARS	3,038	5 YEARS	2,091	5 YEARS
Income tax deductions	**304,500**		**224,080**		**142,230**	

NET EARNINGS AND FUNDS FROM OPERATIONS Net earnings for the year ended December 31, 2007 was $8.2 million ($0.23 per share, basic and $0.23 per share, diluted). During the same period, funds from operations were $83.3 million ($2.34 per share, basic and $2.32 per share, diluted).

On a barrel of oil equivalent basis, funds from operations in 2007 were $29.00 per BOE, down 20% from $36.08 per BOE in 2006. The primary reason for the decrease in 2007 was a result of lower natural gas prices realized during the year. The following table provides detailed unit statistics on a barrel of oil equivalent basis:

UNIT STATISTICS

Year ended December 31,	2007		2006		2005	
	[BOE/D]	[$/BOE]	[BOE/D]	[$/BOE]	[BOE/D]	[$/BOE]
Daily average production	**7,873**		**5,963**		**4,423**	
Sales price		**52.70**		**58.97**		**60.21**
Gain (loss) on financial derivatives		2.68		2.29		(1.80)
Royalties		(11.16)		(10.89)		(10.98)
Production expense		(11.11)		(10.90)		(9.51)
Transportation and selling expense		(0.87)		(0.66)		(0.72)
Operating netback		**32.24**		**38.81**		**37.20**
General and administrative expense		(1.06)		(0.91)		(1.18)
Interest expense		(2.18)		(1.82)		(0.67)
Capital tax		-		-		(0.06)
Funds from operations		**29.00**		**36.08**		**35.29**
Unrealized gain (loss) on financial derivatives		(4.42)		6.27		-
Stock based compensation expense		(0.51)		(0.52)		(0.52)
Depletion, depreciation and amortization		(21.98)		(19.96)		(17.89)
Accretion of asset retirement obligation		(0.11)		(0.24)		(0.13)
Future income tax		0.87		(5.45)		(5.44)
Net earnings		**2.85**		**16.18**		**11.31**

INVESTMENT AND INVESTMENT EFFICIENCIES

CAPITAL EXPENDITURES Celtic is committed to future growth through its strategy to augment strategic oil and gas acquisitions with exploitation upside, and at the same time, implement a full cycle exploration and development program. Since the Company began active oil and gas operations in September 2002, Celtic has completed several acquisitions in order to establish a cash flow platform and an inventory of exploration and development prospects from which the Company can grow through the drill bit. Examples of where Celtic has successfully employed its strategy to acquire an initial position in an area and subsequently expand the area making it core to the Company include Princess/Bantry, Ashmont, Fox Creek and Swan Hills.

During the year ended December 31, 2007, Celtic incurred $135.6 million on exploration and development activity, $45.6 million on property acquisitions and recorded net proceeds of $1.4 million from property dispositions. Drilling and completion operations accounted for $90.9 million and equipment and facility expenditures were $38.1 million. The balance of $6.6 million was spent on land and seismic, building the Company's inventory of prospects for future drilling. Approximately 74% of net wells drilled were development and 26% were exploratory.

The Company's capital expenditures, including acquisitions and dispositions, for the past three years are summarized in the following table:

CAPITAL EXPENDITURES

Year ended December 31,	2007		2006		2005	
	[$ 000s]	[% OF TOTAL]	[$ 000s]	[% OF TOTAL]	[$ 000s]	[% OF TOTAL]
Property, plant and equipment expenditures						
Lease acquisitions and retention	4,909	3	20,996	13	6,676	6
Geological and geophysical activity	1,682	1	2,682	2	2,941	2
Drilling and completion of wells	90,878	51	104,946	64	79,202	67
Facilities, pipeline and well equipment	37,785	21	44,836	27	25,075	21
Office furniture and equipment	312	-	220	-	153	-
	135,566	76	173,680	106	114,047	96
Property, plant and equipment acquisitions	45,636	25	462	-	5,213	4
Property, plant and equipment dispositions	(1,413)	(1)	(10,092)	(6)	(30)	-
Corporate acquisitions	-	-	-	-	-	-
Capital expenditures	**179,789**	**100**	**164,050**	**100**	**119,230**	**100**

UNDEVELOPED LAND As at December 31, 2007, Celtic owned 248,135 net acres of undeveloped land, representing a 5% increase compared to 235,308 net acres at the end of 2006. Approximately 5% of the Company's undeveloped land position is subject to expiry in 2008, if not developed. Celtic holds an average working interest of 76% in its undeveloped lands.

In 2007, Celtic incurred $4.0 million at Alberta Crown land sales acquiring 27,824 net acres of petroleum and natural gas rights at an average cost of $144 per acre; compared to an industry average of $150 per acre. These prices were significantly lower than the previous year in which Celtic spent $20.2 million acquiring 68,950 net acres at an average cost of $293 per acre, compared to the 2006 industry average of $325 per acre. Over 55% of Celtic's 2007 land expenditures were directed towards expanding the Company's acreage position at Kaybob, Alberta, primarily focused on the acquisition of highly prospective Montney rights.

Since inception, Celtic's land acquisition strategy has been focused on building a significant land base of high working interest prospects. During the past two years, Celtic has been successful with this strategy at Kaybob, Alberta, where the Company has an average working interest of 85% in approximately 57,000 acres of developed and undeveloped lands.

Looking ahead to 2008, Celtic will continue its internally generated, prospect-driven land acquisition strategy This strategy will be complemented by third party farm-in arrangements in core exploration areas. Celtic's land acquisition strategy remains focused on building a significant base of high working interest operated prospects, ensuring the Company is in a position to control its capital expenditure program.

The table on the following page summarizes Celtic's land holdings as at December 31, 2007.

UNDEVELOPED LAND HOLDINGS

Year ended December 31,	2007		2006		2005	
[ACRES]	GROSS	NET	GROSS	NET	GROSS	NET
Alberta	321,433	244,915	318,204	232,088	255,720	161,013
British Columbia	4,815	2,819	4,815	2,819	4,815	2,820
Saskatchewan	802	401	802	401	811	406
Total owned undeveloped land	**327,050**	**248,135**	**323,821**	**235,308**	**261,346**	**164,239**
Option lands	-	-	-	-	95,680	64,556
Total controlled undeveloped land	**327,050**	**248,135**	**323,821**	**235,308**	**357,026**	**228,795**

DRILLING During the year ended December 31, 2007, Celtic drilled 65 (56.0 net) wells compared to 83 (62.8 net) wells in the previous year, with an overall success rate of 81% (74% in 2006) on net wells drilled. The Company's average working interest in wells drilled during 2007 increased to 86% compared to an average working interest of 76% in 2006. The split between development drilling and exploratory drilling was 74% (53% in 2006) and 26% (47% in 2006), respectively. The average measured depth of net wells drilled was 2,200 metres, 5% less deep than the average drilling depth of 2,311 metres in 2006. The following table summarizes Celtic's drilling activity in 2007:

DRILLING ACTIVITY

Year ended December 31, 2007	Development Wells		Exploration Wells		Total Wells	
	GROSS	NET	GROSS	NET	GROSS	NET
Oil	6	4.7	1	1.0	7	5.7
Natural gas	31	30.5	7	6.8	38	37.3
Coal bed methane	8	2.6	-	-	8	2.6
Unsuccessful	4	3.4	8	7.0	12	10.4
Total wells	**49**	**41.2**	**16**	**14.8**	**65**	**56.0**
Success rate, based on net wells [%]		**92**		**53**		**81**

RESERVES Celtic retains Sproule Associates Limited ("Sproule"), an independent qualified reserve evaluator to prepare a report on 100% of its oil and gas reserves. The Company has a Reserves Committee which oversees the selection, qualifications and reporting procedures of the independent engineering consultants. Reserves as at December 31, 2007 were determined using the guidelines and definitions set out under National Instrument 51-101 ("NI 51-101"). At December 31, 2007, Celtic's proved plus probable reserves were 33.8 million BOE, up 28% from 26.4 million BOE at the end of 2006.

The table on the following page outlines the change in the Company's reserves year-over-year including discoveries, drilling extensions, improved recoveries, technical revisions, economic factors, dispositions and production.

RESERVES RECONCILIATION

	Oil		Natural Gas		Combined	
	TOTAL PROVED [MBBLS]	PROVED + PROBABLE [MBBLS]	TOTAL PROVED [MMCF]	PROVED + PROBABLE [MMCF]	TOTAL PROVED [MBOE]	PROVED + PROBABLE [MBOE]
Balance, December 31, 2006	**6,770**	**11,634**	**48,999**	**88,327**	**14,937**	**26,355**
Technical revisions	(75)	(1,788)	12,617	164	2,028	(1,761)
Discoveries	61	81	1,691	2,249	343	456
Extensions and improved recoveries	752	1,290	17,029	33,106	3,590	6,808
Economic factors	78	177	266	490	121	259
Acquisitions	958	1,637	10,005	17,356	2,626	4,530
Dispositions	-	-	-	-	-	-
Net additions	1,774	1,397	41,608	53,365	8,708	10,292
Production	(1,134)	(1,134)	(10,439)	(10,439)	(2,874)	(2,874)
Balance, December 31, 2007	**7,410**	**11,897**	**80,168**	**131,253**	**20,771**	**33,773**
Percentage increase in reserves [%]	9	2	64	49	39	28

The Company increased the net present value of proved plus probable reserves, discounted at 10% before tax, to $538.7 million, up 14% from $470.6 million at December 31, 2006. The reserve life index remains strong at 10.0 years compared to 11.5 years at December 31, 2006. At December 31, 2006, proved plus probable reserves were 35% oil and 65% natural gas. The following table outlines a summary of the Company's reserves at December 31, 2007:

SUMMARY OF RESERVES

As at December 31, 2007	OIL [MBBLS]	GAS [MMCF]	COMBINED [MBOE]	Q4 2007 PRODUCTION [BOE/D]	RESERVE LIFE INDEX [YEARS]	NPV 10% BIT [$000s]	NPV PER BOE [$/BOE]
Proved producing	6,640	57,131	16,162	9,213	4.8	323,765	20.03
Total proved	7,410	80,168	20,771	9,213	6.2	376,695	18.14
Total proved plus probable	11,897	131,253	33,773	9,213	10.0	538,719	15.95

Oil prices have steadily increased over the past five years; whereas, natural gas prices have traded in a narrow range, except in 2005 when gas prices were higher due to the impact of supply interruptions resulting from hurricane activity. However, current futures contracts indicate that prices for both oil and gas, are expected to be higher in future years compared to historical averages

The following table outlines forecasted future prices that Sproule has used in their evaluation of the Company's reserves at December 31, 2007:

REFERENCE PRICES

		OIL			GAS		
	CURRENCY EXCHANGE RATE [US$/CA$]	WTI CUSHING OKLAHOMA [US$/BBL]	EDMONTON LIGHT PAR [CA$/BBL]	FORECASTED CELTIC OIL PRICE[1] [CA$/BBL]	HENRY HUB LOUISIANA [US$/MMBTU]	ALBERTA AECO-C SPOT [CA$/MMBTU]	FORECASTED CELTIC GAS PRICE[2] [CA$/MCF]
Historical:							
2003	0.716	31.14	43.23		5.39	6.66	
2004	0.770	41.42	52.91		6.14	6.87	
2005	0.826	56.46	69.29		8.62	8.58	
2006	0.882	66.09	73.30		7.23	7.16	
2007	0.935	72.27	77.06		6.86	6.65	
Five year historical average	**0.826**	**53.48**	**63.16**		**6.85**	**7.18**	
Future Forecasts:							
2008	1.000	89.61	88.17	81.05	7.56	6.51	6.88
2009	1.000	86.01	84.54	77.98	8.27	7.22	7.65
2010	1.000	84.65	83.16	76.30	8.74	7.69	8.17
2011	1.000	82.77	81.26	74.28	8.75	7.70	8.18
2012	1.000	82.26	80.73	73.62	8.66	7.61	8.09
Five year future forecast average	**1.000**	**85.06**	**83.57**	**76.65**	**8.40**	**7.35**	**7.79**

1 Celtic's forecasted average oil price is based on total proved plus probable reserves and does not include heavy oil and NGLs
2 Celtic's forecasted average gas price is based on proved plus probable reserves.

Sproule is forecasting WTI oil prices to average US$85.06 per bbl over the next five years, 59% higher than the average price of US$53.48 per bbl over the past five years. Similarly for natural gas, Henry Hub NYMEX natural gas prices are forecasted to average US$8.40 per mmbtu over the 2008 to 2012 period, an increase of 23% from the average price of US$6.85 per mmbtu during the 2003 to 2007 period.

During 2007, the Company's capital expenditures, net of dispositions, resulted in proved plus probable reserve additions of 10.3 million (10.0 million in 2006) BOE, resulting in finding, development and acquisition ("FD&A") costs of $17.47 ($16.40 in 2006) per BOE, before future capital and $19.27 ($19.56 in 2006) per BOE, including future capital. The recycle ratio is a measure for evaluating the effectiveness of a company's re-investment program. The ratio measures the efficiency of capital investment. It accomplishes this by comparing the operating netback per BOE to that years' reserve FD&A cost per BOE. Since incorporation, Celtic has successfully achieved a recycle ratio of 2.1 times on a proved plus probable basis.

The following table provides detailed calculations relating to FD&A costs and recycle ratios for 2007:

FINDING, DEVELOPMENT AND ACQUISITION COSTS

Year ended December 31,	2007	2006	2005	CUMULATIVE SINCE INCORPORATION
Proved Reserves				
Capital expenditures [$ 000s]	179,789	164,050	119,230	604,397
Change in future capital costs required to develop reserves [$ 000s]	6,998	18,811	7,211	37,850
Total capital costs [$ 000s]	186,787	182,861	126,441	642,247
Reserve additions, net [MBOE]	8,708	6,010	5,631	29,500
FD&A cost, before future capital [$/BOE]	**20.65**	**27.30**	**21.17**	**20.49**
FD&A cost, including future capital [$/BOE]	**21.45**	**30.43**	**22.45**	**21.77**
Operating netback [$/BOE]	**32.24**	**38.81**	**37.20**	**33.56**
Recycle ratio - proved	**1.5**	**1.3**	**1.7**	**1.5**
Proved plus Probable Reserves				
Capital expenditures [$ 000s]	179,789	164,050	119,230	604,397
Change in future capital costs required to develop reserves [$ 000s]	18,508	31,690	13,856	72,106
Total capital costs [$ 000s]	198,297	195,740	133,086	676,503
Reserve additions, net [MBOE]	10,292	10,005	9,089	42,502
FD&A cost, before future capital [$/BOE]	**17.47**	**16.40**	**13.12**	**14.22**
FD&A cost, including future capital [$/BOE]	**19.27**	**19.56**	**14.64**	**15.92**
Operating netback [$/BOE]	**32.24**	**38.81**	**37.20**	**33.56**
Recycle ratio - proved plus probable	**1.7**	**2.0**	**2.5**	**2.1**

Celtic's 2007 capital investment program replaced 2007 production by a factor of 3.0 (2.8 in 2006) times on a proved basis and 3.6 (4.6 in 2006) times on a proved plus probable basis. The following table summarizes production replacement for 2007:

PRODUCTION REPLACEMENT

	PROVED			PROVED PLUS PROVABLE		
	OIL [MBBLS]	GAS [MMCF]	COMBINED [MBOE]	OIL [MBBLS]	GAS [MMCF]	COMBINED [MBOE]
Reserve additions, including revisions	1,774	41,608	8,709	1,397	53,365	10,291
2007 Production	1,134	10,439	2,874	1,134	10,439	2,874
Production replacement ratio	**1.6**	**4.0**	**3.0**	**1.2**	**5.1**	**3.6**

NET ASSET VALUE Celtic's net asset value at December 31, 2007, discounting the present value of reserves at 10% before tax, increased to $477.9 million ($526.1 million using an 8% discount rate, before tax), up 12% from $426.4 million at December 31, 2006. On a per share basis, net asset value decreased by 4% to $11.80 per share ($12.99 per share using an 8% discount rate, before tax). The present value of petroleum and natural gas ("P&NG") reserves were determined by Sproule in their year-end evaluation report. Undeveloped land at December 31, 2007 was valued at an average price of $182 per acre.

The components of net asset value are summarized in the following table:

NET ASSET VALUE

Forecast Prices At December 31, [$ 000s]	2007	2007	2006
DISCOUNT RATE [%]	8	10	10
Present value of P&NG reserves, discounted, before tax	586,964	538,719	470,559
Undeveloped land	45,195	45,195	32,949
Bank debt, net of working capital	(136,249)	(136,249)	(98,236)
Proceeds from exercise of stock options	30,197	30,197	21,097
Net asset value	**526,107**	**477,862**	**426,369**
Diluted common shares outstanding [000s]	40,492	40,492	34,810
Net asset value per share [$/SHARE]	**12.99**	**11.80**	**12.25**

CAPITAL RESOURCES AND LIQUIDITY

MARKET CAPITALIZATION The Company's total capitalization increased 2% to $600.4 million at December 31, 2007. Market value of common shares represented 70% of total capitalization, while debt and working capital represented 23% of total capitalization. The following table summarizes the Company's capitalization:

CAPITALIZATION

At December 31,	2007		2006		2005	
Common shares outstanding [000s]	37,666		32,180		28,973	
Share price [$ LAST PRICE TRADED AT IN THE YEAR]	11.20		13.91		12.40	
[$ 000s, EXCEPT PER SHARE AMOUNTS]		[%]		[%]		[%]
Market capitalization	421,859	70	447,624	76	359,265	80
Bank debt, net of working capital	136,249	23	98,236	17	63,426	14
Asset retirement obligation	5,719	1	4,885	1	4,294	1
Future income taxes	36,596	6	36,162	6	23,864	5
Total capitalization	**600,423**	**100**	**586,907**	**100**	**450,849**	**100**

At December 31, 2007, the Company had $119.9 million outstanding on its credit facility. Total debt, including working capital deficiency was $136.2 million, representing approximately 1.6 times 2007 funds from operations and approximately 1.1 times forecasted 2008 funds from operations.

KEY DEBT RATIOS

At December 31,	2007		2006		2005	
	[$ 000s]	RATIO	[$ 000s]	RATIO	[$ 000s]	RATIO
Debt to funds from operations ratio:						
Total debt	136,249		98,236		63,426	
Funds from operations	83,340		78,541		56,969	
Funds from operations - 2008 forecast	120,000					
Debt to funds from operations - trailing		1.6		1.3		1.1
Debt to funds from operations - forward		**1.1**		**1.2**		**0.8**
Asset coverage ratio:						
Total assets	490,431		373,882		242,113	
Total debt	136,249		98,236		63,426	
Asset coverage		**3.6**		**3.8**		**3.8**
Debt to equity ratio:						
Total debt	136,249		98,236		63,426	
Shareholders' equity	281,463		200,029		125,847	
Debt/equity		**0.5**		**0.5**		**0.5**

SOURCE OF FUNDS Investment funding for capital expenditures incurred in 2007 was provided by proceeds from equity financings, bank debt and cash provided by operating activities.

In February 2007, the Company issued 1.5 million common shares on a flow-through basis by way of private placement, at a price of $16.65 per share and in June 2007, Celtic completed the issuance of 3.2 million common shares by way of private placement, at a price of $14.35 per share. These equity offerings resulted in gross proceeds of $70.9 million.

The Company has in place a committed term credit facility with Canadian financial institutions. The maximum amount available to be drawn under this facility at December 31, 2007 was $165.0 million. At December 31, 2007, Celtic had drawn $119.9 million, leaving sufficient unused credit lines available to fund on-going capital expenditures. Repayments of principal are not required provided that the borrowings under the facility do not exceed the authorized borrowing amount and the Company is in compliance with all covenants, representations and warranties. The maximum amount available under this credit facility may increase after the Company's lenders complete their annual review in May 2008.

In order to fund all capital expenditures incurred in 2007, the Company augmented its equity financing and bank borrowings by generating $85.1 million in cash provided by operating activities for the year ended December 31, 2007.

Celtic expects to fund future capital expenditures through the use of a combination of cash provided by operating activities and bank debt, supplemented by new equity share offerings, as required.

WORKING CAPITAL The capital intensive nature of Celtic's activities may create a working capital deficiency position during periods with high levels of capital investment. However, during such periods, the Company maintains sufficient unused bank credit lines to satisfy such working capital deficiencies. At December 31, 2007, the working capital amount plus outstanding bank debt represented 83% of the Company's maximum authorized bank borrowing credit limit.

The oil and gas industry has a pre-arranged monthly clearing day for payment of revenues from all buyers of oil and natural gas. This occurs on the 25th day following the month of sale. As a result, the Company's production revenues are collected in an orderly fashion. Celtic monitors its revenue counterparty credit positions to mitigate any potential credit losses. To the extent that the Company has joint venture partners in its activities, it must collect the partners' share of capital expenditures and operating expenses on a monthly basis. Exceptions are in the event that the partners' share of a capital project is a significant amount. In this case, Celtic will collect such amounts from its partners in advance of expenditures taking place in accordance with standard industry operating procedures. At December 31, 2007, the Company did not have any material accounts receivable that were deemed uncollectible.

Accounts payable consist of amounts payable to suppliers relating to head office and field operating and investing activities. These invoices are processed within the Company's normal payment period.

Celtic actively manages the pace of its capital spending program by monitoring forecasted production and commodity prices and resulting cash flows. Should circumstances affect cash flow in a detrimental way, the Company is capable of reducing capital investment levels.

SHARE INFORMATION The Company is authorized to issue an unlimited number of common shares and an unlimited number of preferred shares. As at December 31, 2007, there were 37.7 million common shares outstanding (as at March 7, 2008, there were 37.7 million common shares outstanding). There are no preferred shares outstanding.

As at December 31, 2007, directors, employees and consultants have been granted options to purchase 2.8 million common shares of the Company at an average exercise price of $10.69 per share. Detailed information regarding the Company's stock options outstanding is contained in the notes to the financial statements.

The Company's common shares trade on the Toronto Stock Exchange ("TSX") under the symbol "CLT". The table on the following page outlines Celtic's common share trading activity by quarter during the years 2007, 2006 and 2005.

SHARE TRADING ACTIVITY (CLT)

	Q1	Q2	Q3	Q4	2007
High [$]	14.00	15.23	14.75	13.75	15.23
Low [$]	11.51	12.41	12.25	10.60	10.60
Close [$]	12.90	14.51	13.48	11.20	11.20
Volume traded [000s]	1,553	4,586	2,701	2,979	11,819
Value traded [$ 000s]	19,452	63,028	37,546	35,601	155,626
Weighted average trading price [$]	12.52	13.74	13.90	11.95	13.17

	Q1	Q2	Q3	Q4	2006
High [$]	13.02	14.80	14.39	14.00	14.80
Low [$]	11.06	11.90	12.15	11.83	11.06
Close [$]	12.69	12.77	12.70	13.91	13.91
Volume traded [000s]	3,100	1,882	2,855	1,644	9,482
Value traded [$ 000s]	38,372	24,748	38,454	20,744	122,319
Weighted average trading price [$]	12.38	13.15	13.47	12.62	12.90

	Q1	Q2	Q3	Q4	2005
High [$]	12.45	11.75	13.50	12.91	13.50
Low [$]	9.00	8.91	10.50	11.10	8.91
Close [$]	11.00	11.15	12.90	12.40	12.40
Volume traded [000s]	4,172	3,986	4,627	3,677	16,462
Value traded [$ 000s]	45,333	42,390	56,662	44,290	188,675
Weighted average trading price [$]	10.87	10.63	12.25	12.05	11.46

FUTURE COMMITMENTS – FINANCIAL INSTRUMENTS The Company may, from time to time, enter into fixed price contracts and derivative financial instruments with respect to oil and gas sales, in order to secure a certain amount of cash flow to protect a level of capital spending. As at December 31, 2007, Celtic has the following fixed price commitments, in place, to sell oil and gas production:

The following is a summary of oil sales price derivative contracts in effect as at December 31, 2007, that has fixed future sales prices (fixed oil prices are based on the West Texas Intermediate ("WTI") Index):

Daily quantity	Remaining term of contract	Fixed price per barrel [BBL]
500 bbls/d	January 1 to December 31, 2008	$89.00
500 bbls/d	January 1 to December 31, 2008	$88.00
300 bbls/d	January 1 to December 31, 2008	US$92.50
500 bbls/d	January 1 to December 31, 2008	US$70.00

The following is a summary of natural gas sales price derivative contracts in effect as at December 31, 2007, that has fixed future sales prices (fixed natural gas prices are based on the New York Mercantile Exchange ("NYMEX") Index):

Daily quantity	Remaining term of contract	Fixed price per mmbtu (NYMEX)
6,500 mmbtu/d (costless collar)	January 1 to December 31, 2008	US$8.00 (floor) US$9.05 (cap)

The following is a summary of natural gas sales price derivative contracts in effect as at December 31, 2007, that has fixed future sales prices (fixed natural gas prices are based on the AECO-C Index):

Daily quantity	Remaining term of contract	Fixed price per GJ (AECO)
5,000 GJ/d	January 1 to October 31, 2008	$ 7.43
20,000 GJ/d	January 1 to October 31, 2008	$ 7.02

CONTRACTUAL OBLIGATIONS Celtic has a committed term credit facility with Canadian financial institutions. The authorized borrowing amount under this facility as at December 31, 2007 was $165.0 million, of which $119.9 million was outstanding. Interest under this facility is payable monthly. Additional disclosure relating to bank debt is provided in the notes to the financial statements.

From time to time, the Company enters into agreements to transport and market oil and gas production. In addition, the Company has entered into agreements with third parties that provides employees with access to specialized computer software and information including production and reserves data, geological data, accounting systems and land management systems.

As a normal course of business, the Company leases office space, vehicles for field personnel and office equipment such as computers, printers and photocopiers.

CONTRACTUAL OBLIGATIONS AND COMMITMENTS

Years ended December 31, ($ 000s)	2008	2009	2010	2011	Total
Operating lease - office building	568	568	568	189	1,893
Operating lease - vehicles	137	57	-	-	194
Firm transportation agreements	252	92	-	-	344
Exploration and development expenditures	12,481	-	-	-	12,481
Bank debt	119,900	-	-	-	119,900
Total	**133,338**	**717**	**568**	**189**	**134,812**

RELATED PARTY AND OFF-BALANCE SHEET TRANSACTIONS The Company has retained the law firm of Borden Ladner Gervais LLP (BLG) to provide Celtic with legal services. William C. Guinan, a director, chairman and corporate secretary of Celtic is a partner of this law firm. During 2007, the Company incurred $260,200 in costs with BLG The Company expects to continue using the services of this law firm from time to time.

Celtic was not involved in any off-balance sheet transactions in the years ended December 31, 2006 and 2007.

SUPPLEMENTAL QUARTERLY INFORMATION

The Company has been successful in providing strong growth in funds from operations and daily average production. The following tables summarize key financial and operating information by quarter:

QUARTERLY FINANCIAL INFORMATION

[$ 000s, unless otherwise indicated]

2007	Q1	Q2	Q3	Q4	Total
Revenue, net of royalties	18,518	28,077	36,664	31,113	114,372
Funds from operations	22,045	19,244	18,805	23,246	83,340
Basic [$/SHARE]	0.68	0.56	0.50	0.62	2.34
Diluted [$/SHARE]	0.67	0.55	0.50	0.61	2.32
Net earnings (loss)	(2,850)	2,957	4,584	3,507	8,198
Basic [$/SHARE]	(0.09)	0.09	0.12	0.09	0.23
Diluted [$/SHARE]	(0.09)	0.09	0.12	0.09	0.23
Total assets	405,249	465,151	479,026	490,431	490,431
Bank debt, net of working capital	117,188	119,367	128,027	136,249	136,249

2006	Q1	Q2	Q3	Q4	Total
Revenue, net of royalties	27,782	24,632	37,757	33,091	123,262
Funds from operations	20,538	18,008	20,812	19,183	78,541
Basic [$/SHARE]	0.71	0.60	0.70	0.60	2.57
Diluted [$/SHARE]	0.69	0.59	0.68	0.58	2.50
Net earnings	7,301	5,481	15,850	6,599	35,231
Basic [$/SHARE]	0.25	0.18	0.53	0.21	1.15
Diluted [$/SHARE]	0.24	0.18	0.52	0.20	1.12
Total assets	288,839	308,890	354,768	373,882	373,882
Bank debt, net of working capital	85,107	83,452	85,251	98,236	98,236

2005	Q1	Q2	Q3	Q4	Total
Revenue, net of royalties	14,099	13,645	22,186	26,647	76,577
Funds from operations	10,489	10,724	17,082	18,674	56,969
Basic [$/SHARE]	0.41	0.39	0.59	0.65	2.05
Diluted [$/SHARE]	0.39	0.38	0.57	0.62	1.98
Net earnings	3,018	2,455	5,729	7,062	18,264
Basic [$/SHARE]	0.12	0.09	0.20	0.24	0.66
Diluted [$/SHARE]	0.11	0.09	0.19	0.24	0.64
Total assets	155,257	178,574	207,074	242,113	242,113
Bank debt, net of working capital	43,277	29,589	42,003	63,426	63,426

QUARTERLY OPERATING INFORMATION

2007	Q1	Q2	Q3	Q4	Total
Production					
Oil [BBLS/D]	3,147	2,947	3,102	3,230	3,107
Natural gas [MCF/D]	18,975	24,398	34,871	35,898	28,599
Combined [BOE/D]	6,310	7,013	8,914	9,213	7,873
Production per million shares [BOE/D]	192	205	238	245	222
Realized sales prices, after derivatives					
Oil [$/BBL]	65.77	66.54	69.84	73.30	68.95
Natural gas [$/MCF]	11.31	7.96	6.20	7.29	7.76
Combined [$/BOE]	66.81	55.64	48.55	54.13	55.38
Operating netbacks, after derivatives					
Oil [$/BBL]	37.65	40.55	38.23	38.71	38.76
Natural gas [$/MCF]	7.92	4.80	3.19	4.32	4.67
Combined [$/BOE]	42.60	33.72	25.78	30.44	32.24

2006	Q1	Q2	Q3	Q4	Total
Production					
Oil [BBLS/D]	3,617	3,187	3,048	3,290	3,284
Natural gas [MCF/D]	14,322	13,134	18,759	18,001	16,072
Combined [BOE/D]	6,004	5,376	6,175	6,290	5,963
Production per million shares [BOE/D]	207	181	197	196	195
Realized sales prices, after derivatives					
Oil [$/BBL]	62.11	63.98	70.99	58.68	63.78
Natural gas [$/MCF]	11.40	9.31	8.31	10.10	9.71
Combined [$/BOE]	64.63	60.69	60.31	59.59	61.26
Operating netbacks, after derivatives					
Oil [$/BBL]	37.12	39.86	42.56	31.07	37.54
Natural gas [$/MCF]	7.59	6.70	6.02	6.83	6.75
Combined [$/BOE]	40.49	40.01	39.30	35.79	38.81

2005	Q1	Q2	Q3	Q4	Total
Production					
Oil [BBLS/D]	2,269	2,067	2,833	2,915	2,524
Natural gas [MCF/D]	8,856	10,101	13,485	13,071	11,396
Combined [BOE/D]	3,745	3,751	5,081	5,094	4,423
Production per million shares [BOE/D]	145	136	176	176	159
Realized sales prices, after derivatives					
Oil [$/BBL]	54.01	59.08	64.12	57 49	58 91
Natural gas [$/MCF]	8.33	7.61	9.15	12 51	9.63
Combined [$/BOE]	52.41	53.03	60 03	65.00	58.41
Operating netbacks, after derivatives					
Oil [$/BBL]	35.80	34 99	40.32	35 37	36 79
Natural gas [$/MCF]	5.05	5.26	5.83	8.38	6 29
Combined [$/BOE]	33.64	33.42	37.94	41.76	37.20

Factors that have caused variations over the quarters:

- The majority of Celtic's production growth has been the result of the Company's successful exploration and development drilling activities:
  - The Company estimates that approximately 80% of fourth quarter 2007 production came from exploration and development activities and the balance from acquisitions.
- In addition to drilling activities, oil and gas property acquisitions completed in 2005 and 2007 have also contributed to production growth:
  - In 2005, Celtic completed the acquisition of oil and gas properties in the Virginia Hills area of west central Alberta for approximately $2.5 million, adding approximately 350 BOE/d (73% oil and 27% natural gas).
  - In 2007, Celtic completed the acquisition of complementary liquids-rich natural gas properties in the Kaybob South area of west central Alberta for approximately $46.0 million, adding approximately 1,040 BOE/d (63% natural gas and 37% natural gas liquids).
- Revenue, funds from operations and earnings growth is primarily the result of production growth and increases in commodity prices.

BUSINESS RISKS

Celtic's exploration and production activities are concentrated in the Western Canadian Sedimentary Basin, where activity is highly competitive and includes a variety of different sized companies ranging from smaller junior producers, intermediate and senior producers and royalty trust organizations, to the much larger integrated petroleum companies. Celtic is subject to a number of risks which are also common to other organizations involved in the oil and gas industry. Such risks include finding and developing oil and gas reserves at economic costs, estimating amounts of recoverable reserves, production of oil and gas in commercial quantities, marketability of oil and gas produced, fluctuations in commodity prices, financial and liquidity risks and environmental and safety risks.

In order to reduce exploration risk, Celtic employs highly qualified and motivated professional employees who have demonstrated the ability to generate quality proprietary geological and geophysical prospects. To maximize drilling success,

Celtic explores in areas that afford multi-zone prospect potential, targeting a range of shallower low to moderate risk prospects with some exposure to select deeper high-risk prospects with high-reward opportunities.

Celtic has retained an independent engineering consulting firm that assists the Company in evaluating recoverable amounts of oil and gas reserves. Values of recoverable reserves are based on a number of variable factors and assumptions such as commodity prices, projected production, future production costs and government regulation. Such estimates may vary from actual results.

The Company mitigates its risk related to producing hydrocarbons through the utilization of the most advanced technology and information systems. In addition, Celtic strives to operate the majority of its prospects, thereby maintaining operational control. The Company does rely on its partners in jointly owned properties that Celtic does not operate.

Celtic is exposed to market risk to the extent that the demand for oil and gas produced by the Company exists within Canada and the United States. External factors beyond the Company's control may affect the marketability of oil and gas produced. These factors include commodity prices and variations in the Canada-United States currency exchange rate, which in turn respond to economic and political circumstances throughout the world. Oil prices are affected by worldwide supply and demand fundamentals while natural gas prices are affected by North American supply and demand fundamentals. Celtic may periodically use futures and options contracts to hedge its exposure against the potential adverse impact of commodity price volatility.

Exploration and production for oil and gas is very capital intensive. As a result, the Company relies on equity markets as a source of new capital. In addition, Celtic utilizes bank financing to support on-going capital investment. Funds from operations also provide Celtic with capital required to grow its business. Equity and debt capital is subject to market conditions and availability may increase or decrease from time to time. Funds from operations also fluctuate with changing commodity prices.

Oil and gas exploration and production can involve environmental risks such as pollution of the environment and destruction of natural habitat, as well as safety risks such as personal injury. The Company conducts its operations with high standards in order to protect the environment and the general public. Celtic maintains current insurance coverage for comprehensive and general liability as well as limited pollution liability. The amount and terms of this insurance are reviewed on an ongoing basis and adjusted as necessary to reflect current corporate requirements, as well as industry standards and government regulations.

BUSINESS OUTLOOK

ADVISORY REGARDING FORWARD-LOOKING STATEMENTS Certain information with respect to Celtic contained herein, including management's assessment of future plans and operations, contains forward-looking statements. These forward-looking statements are based on assumptions and are subject to numerous risks and uncertainties, certain of which are beyond Celtic's control, including the impact of general economic conditions, industry conditions, volatility of commodity prices, currency exchange rate fluctuations, imprecision of reserve estimates, environmental risks, competition from other explorers, stock market volatility and ability to access sufficient capital. As a result, Celtic's actual results, performance or achievement could differ materially from those expressed in, or implied by, these forward-looking statements and, accordingly, no assurance can be given that any events anticipated by the forward-looking statements will transpire or occur. In addition, the reader is cautioned that historical results are not necessarily indicative of future performance.

2008 GUIDANCE Celtic remains optimistic about its future prospects. Since commencing operations, the Company was successful in establishing a production base during the early months that provides a cash flow stream that can be re-invested into Celtic's ongoing exploration and development activity. Celtic is opportunity driven and is confident that it can continue to grow the Company's production base by building on its current inventory of development prospects and by adding new exploration prospects. Celtic will endeavour to maintain a high quality product stream that on a historical basis receives a superior price with reasonably low production costs. In addition, the Company takes advantage of royalty incentive programs in order to further increase netbacks. Celtic will continue to focus its exploration efforts in areas of multi-zone potential.

Celtic's Board of Directors has approved a capital expenditure budget in the amount of $120 million for 2008. This capital spending will be financed by funds from operations and available bank credit lines.

After forecasting risked production discoveries, timing of production on-stream dates resulting from the Company's planned capital expenditures for 2008 and estimated decline rates on existing volumes, Celtic expects production in 2008 to average between 10,500 and 10,700 BOE/d (34% oil and 66% gas). This represents a 33% to 36% increase from average production of 7,873 BOE/d in 2007.

Political turmoil in major oil producing regions around the world continues to remain in the headlines and could potentially put a strain on stable world oil supply in the future. The insatiable appetite for oil demonstrated by countries such as India and China, in the past two years, could continue and therefore keep demand for oil growing. As a result of these and other factors, Celtic expects oil prices to be higher in 2008 compared to 2007. Natural gas demand in North America in 2007 was higher than in 2006 and appears to be increasing, particularly in the area of electric power. However, increased demand was offset by increases in supply in 2007, mainly due to larger LNG imports. However, natural gas prices in 2008 should benefit from the reduced supply resulting from a slow down in natural gas drilling in Canada and a diversion of LNG's to Europe and Asia, as has been the case in the past few months.

The Company's commodity price assumptions for 2008 are US$84.00 per barrel for WTI oil, US$8.50 per mmbtu for NYMEX natural gas and a US/Canadian exchange rate of US$1.000. These prices compare to 2007 average prices of US$72.34 per barrel for WTI oil, US$6.92 per mmbtu for NYMEX natural gas and a US/Canadian exchange rate of US$0.931. Given the strength of the Canadian dollar, actual realized oil and gas prices are affected negatively.

After giving effect to the aforementioned production and commodity price assumptions and taking into effect commodity risk price management contracts in place (as outlined in detail in the notes to the financial statements), funds from operations for 2008 is forecasted to be approximately $120.0 million or $3.19 per share ($3.11 per share, diluted) and net earnings is forecasted to be approximately $19.5 million or $0.52 per share ($0.51 per share, diluted). Changes in forecasted commodity prices and variances in production estimates can have a significant impact to estimated funds from operations and net earnings. Please refer to the advisory regarding forward-looking statements shown above.

Bank debt, net of working capital, is estimated to reach $136.9 million by the end of 2008 or approximately 1.1 times forecasted 2008 funds from operations.

Celtic's capital expenditure budget for 2008 will see the Company participate at high working interests in the drilling of approximately 58 to 62 wells during the year, of which approximately 35 wells will be horizontals. Celtic continues to pursue property acquisitions that would complement its existing asset base and completion of such acquisitions would be over and above the Company's planned capital expenditure budget.

Celtic is excited about the growth prospects being generated in the Company and remains optimistic about the Company's ability to deliver continued per share growth in production, reserves, net asset value, earnings and funds from operations. Given the Company's strong inventory of drilling locations, we look forward to continued growth in 2008.

ADDITIONAL INFORMATION

Additional information relating to Celtic, including the Company's Annual Information Form ("AIF") is filed on SEDAR and can be viewed on their website at www.sedar.com. Copies of the AIF can also be obtained by contacting Sadiq H. Lalani, Vice President, Finance and Chief Financial Officer at Celtic Exploration Ltd., Suite 500, 505 Third Street SW, Calgary, Alberta, Canada, T2P 3E6. Further information relating to the Company is also available on its website at www.celticex.com.

MANAGEMENT'S REPORT

Management has prepared the accompanying financial statements of Celtic Exploration Ltd. in accordance with Canadian generally accepted accounting principles. Financial information presented throughout this annual report is consistent with that shown in the financial statements

Management is responsible for the integrity of the financial information. Where appropriate, management has made informed judgments and estimates in accounting for transactions which affect the current accounting period but cannot be finalized with certainty until future periods. Internal control systems are designed and maintained to provide reasonable assurance that assets are safeguarded from loss or unauthorized use and to produce reliable accounting records for financial reporting purposes.

PricewaterhouseCoopers LLP was appointed by the Company's shareholders to perform an examination of the corporate and accounting records so as to express an opinion on the financial statements. Their examination included a review and evaluation of Celtic's internal control systems and included such tests and procedures, as they considered necessary, to provide reasonable assurance that the financial statements are presented fairly in accordance with Canadian generally accepted accounting principles

The Board of Directors is responsible for ensuring that management fulfills its responsibilities for financial reporting and internal control. The Board exercises this responsibility with the assistance of the Audit Committee. This Committee, consisting of non-management directors, meets with management and independent auditors to ensure that each group is properly discharging its responsibilities and to discuss adequacy of internal controls, accounting policies and financial reporting matters. The Audit Committee has reviewed the financial statements and has reported thereon to the Board of Directors. The Board has approved the financial statements for issuance to the shareholders.

DAVID J. WILSON
President and Chief Executive Officer

SADIQ H. LALANI
Vice President, Finance and Chief Financial Officer

AUDITORS' REPORT

To the Shareholders of Celtic Exploration Ltd.

We have audited the balance sheets of Celtic Exploration Ltd. as at December 31, 2007 and 2006, and the statements of operations, retained earnings and accumulated other comprehensive income, and cash flows for the years ended December 31, 2007 and 2006. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these financial statements present fairly, in all material respects, the financial position of the Company as at December 31, 2007 and 2006, and the results of its operations and its cash flows for the years ended December 31, 2007 and 2006, in accordance with Canadian generally accepted accounting principles.

PricewaterhouseCoopers LLP

CHARTERED ACCOUNTANTS
MARCH 7, 2008

BALANCE SHEET

As at December 31 [$ 000s]	2007	2006
ASSETS		
Current assets		
Cash and cash equivalents	$ 3,082	$ 824
Accounts receivable	25,751	19,278
Prepaid expenses	646	833
Financial derivative contracts [NOTE 9]	925	13,635
	30,404	34,570
Other assets	4,281	1,713
Property, plant and equipment [NOTE 2]	455,746	337,599
	$ 490,431	$ 373,882
LIABILITIES		
Current liabilities		
Accounts payable and accrued liabilities	$ 46,480	$ 26,804
Current portion of future income taxes	273	4,202
Bank debt [NOTE 3]	119,900	101,800
	166,653	132,806
Asset retirement obligation [NOTE 4]	5,719	4,885
Future income taxes	36,596	36,162
	$ 208,968	$ 173,853
SHAREHOLDERS' EQUITY		
Share capital [NOTE 5]	$ 200,180	$ 127,841
Contributed surplus [NOTE 5]	3,364	2,467
Retained earnings and accumulated other comprehensive income	77,919	69,721
	$ 281,463	$ 200,029
	$ 490,431	$ 373,882

ON BEHALF OF THE BOARD OF DIRECTORS:

Director

Director

STATEMENT OF OPERATIONS, RETAINED EARNINGS AND ACCUMULATED OTHER COMPREHENSIVE INCOME

Years ended December 31, [$ 000s, EXCEPT PER SHARE AMOUNTS]	2007	2006
STATEMENT OF OPERATIONS		
REVENUE		
Oil and natural gas	$ 151,443	$ 128,344
Royalties	(32,062)	(23,710)
Realized gain on financial derivatives	7,702	4,993
Unrealized gain (loss) on financial derivatives [NOTE 9]	(12,711)	13,635
	$ 114,372	$ 123,262
EXPENSES		
Production	$ 31,933	$ 23,712
Transportation and selling	2,509	1,438
Interest	6,268	3,959
General and administrative	3,033	1,977
Stock based compensation [NOTE 5D]	1,453	1,121
Depletion, depreciation and amortization [NOTE 2]	63,177	43,433
Accretion of asset retirement obligation [NOTE 4]	320	526
	$ 108,693	$ 76,166
Earnings before taxes	$ 5,679	$ 47,096
Provision for (recovery of) future income taxes	(2,519)	11,865
Net earnings and comprehensive income	$ 8,198	$ 35,231
Earnings per share		
Basic	$ 0.23	$ 1.15
Diluted [NOTE 7]	0.23	1.12

STATEMENT OF RETAINED EARNINGS AND ACCUMULATED OTHER COMPREHENSIVE INCOME

	2007	2006
Retained earnings and accumulated other comprehensive income, beginning of period	$ 69,721	$ 34,490
Net earnings and comprehensive income	8,198	35,231
Retained earnings and accumulated other comprehensive income, end of period	$ 77,919	$ 69,721

The accompanying notes form an integral part of these financial statements

STATEMENT OF CASH FLOWS

Years ended December 31, [$ 000s]		2007		2006
OPERATING ACTIVITIES				
Net earnings	$	8,198	$	35,231
Items not affecting cash:				
Depletion, depreciation and amortization		63,177		43,433
Accretion of asset retirement obligation		320		526
Stock based compensation		1,453		1,121
Unrealized loss (gain) on financial derivatives		12,711		(13,635)
Future income taxes		(2,519)		11,865
Funds from operations	$	83,340	$	78,541
Settlement of asset retirement obligations		(1,021)		(646)
Change in non-cash operating working capital [NOTE 9]		2,772		3,739
Cash provided by operating activities	$	85,091	$	81,634
FINANCING ACTIVITIES				
Increase in bank debt	$	18,100	$	60,100
Issue of common shares, net of costs		70,807		42,464
Cash provided by financing activities	$	88,907	$	102,564
INVESTING ACTIVITIES				
Property, plant and equipment expenditures	$	(135,566)	$	(173,680)
Property, plant and equipment acquisitions		(45,636)		(462)
Property, plant and equipment dispositions		1,413		10,092
Change in other assets		(2,568)		(553)
Change in non-cash investing working capital [NOTE 9]		10,617		(20,583)
Cash used in investing activities	$	(171,740)	$	(185,186)
Net change in cash and cash equivalents	$	2,258	$	(988)
Cash and cash equivalents, beginning of period		824		1,812
Cash and cash equivalents, end of period	$	3,082	$	824

The accompanying notes form an integral part of these financial statements

[illegible]

For the years ended December 31, 2007 and December 31, 2006
[ALL TABULAR AMOUNTS IN 000s, UNLESS OTHERWISE STATED]

[NOTE 1] SIGNIFICANT ACCOUNTING POLICIES

NATURE OF BUSINESS Celtic Exploration Ltd. ("Celtic" or the "Company") was incorporated under the Business Corporations Act (Alberta) on April 16, 2002. Celtic is an oil and natural gas exploration, development and production company based in Calgary, Alberta, Canada. The Company's operations are focused in Western Canada, primarily in Alberta.

BASIS OF PRESENTATION These financial statements are stated in Canadian dollars and have been prepared in accordance with Canadian generally accepted accounting principles ("GAAP"). The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements as well as the reported amounts of revenues, expenses and cash flows during the period. Actual results could differ from these estimates.

MEASUREMENT UNCERTAINTY The amounts recorded for stock based compensation, depletion, depreciation and amortization of assets, the provision for asset retirement obligation costs and the provision for future income taxes are based on estimates. In addition, the ceiling test calculation is based on estimates of proved reserves, production rates, oil and gas prices, future costs and other relevant assumptions. By their nature, these estimates are subject to measurement uncertainty and the effect on the financial statements of changes in such estimates in future periods could be material.

JOINT INTERESTS A portion of the Company's exploration, development and production activities is conducted jointly with others. These financial statements reflect only the Company's proportionate interest in such activities.

CASH AND CASH EQUIVALENTS Cash and cash equivalents include cash on hand, demand deposits and investments in highly liquid money market instruments which are convertible to known amounts of cash in less than three months.

FINANCIAL INSTRUMENTS AND DERIVATIVES GAAP prescribes when a financial asset, financial liability or non-financial derivative is to be recognized on the balance sheet and at what amount, requiring fair value or cost-based measures under different circumstances. All financial instruments must be classified as one of the following five categories: loans and receivables; held-to-maturity investments; held-for-trading instruments; available-for-sale financial assets; or other financial liabilities. All financial instruments, with the exception of loans and receivables, held-to-maturity investments and other financial liabilities which are recorded at amortized cost, are reported on the balance sheet at fair value. Subsequent measurement and changes in fair value will depend on their initial classification. Available-for-sale financial assets are measured at fair value and unrealized gains or losses resulting from changes in fair value are recorded in other comprehensive income until the investment is de-recognized or impaired at which time the amounts would be recorded in earnings.

All derivative instruments, including embedded derivatives, are recorded on the balance sheet at fair value unless they qualify for the normal sale and purchase exception. All changes in fair value are included in earnings unless cash flow hedge or net investment accounting is used, in which case changes in fair value are recorded in other comprehensive income, to the extent the hedge is effective, and in earnings, to the extent it is ineffective.

PROPERTY, PLANT AND EQUIPMENT The Company follows the full cost method of accounting whereby all costs relating to the exploration and development of petroleum and natural gas reserves are capitalized. Such costs include land acquisition, geological and geophysical, drilling of productive and non-productive wells, production equipment and facilities, carrying costs directly related to unproved properties and costs related to acquisition of petroleum and natural gas assets directly or by means of a business combination. These capitalized costs along with estimated future capital expenditures to be incurred in order to develop proved reserves, are depleted and depreciated on a unit of production basis using estimated proved petroleum and natural gas reserves as

evaluated by independent engineers. For purposes of this calculation, petroleum and natural gas reserves are converted to a common unit of measurement on the basis of their relative energy content where six thousand cubic feet of gas equates to one barrel of oil. Costs of acquiring and evaluating unproved properties are excluded from costs subject to depletion and depreciation until it is determined whether proved reserves are attributable to the properties or impairment occurs.

Gains or losses on the disposition of properties are not recognized unless the proceeds on disposition result in a change of 20 percent or more in the depletion rate.

Depreciation of furniture and office equipment is provided using the declining balance method at a rate of 25 percent.

The net amount at which petroleum and natural gas properties are carried is subject to a cost recovery test (the "ceiling test"). Under this test, an estimate is made of the ultimate recoverable amount from undiscounted future net cash flows based on proved reserves, which are determined by using forecasted future prices, plus unproved properties. If the carrying amount exceeds the ultimate recoverable amount, an impairment loss is recognized in net earnings. The impairment loss is limited to the amount by which the carrying amount exceeds: (i) the sum of the fair value of proved and probable reserves; and (ii) the costs of unproved properties that have been subject to a separate impairment test and contain no probable reserves.

ASSET RETIREMENT OBLIGATIONS Estimated future costs relating to retirement obligations associated with oil and gas well sites and facilities are recognized as a liability, at fair value. The asset retirement cost, equal to the fair value of the retirement obligation, is capitalized as part of the cost of the related asset. These capitalized costs are amortized on a unit-of-production basis, consistent with depletion and depreciation. The liability is adjusted at each reporting period to reflect the passage of time, with the accretion charged to earnings. Actual costs incurred upon settlement of the obligations are charged against the liability.

FUTURE INCOME TAXES The Company follows the liability method of accounting for income taxes. Temporary differences arising from the differences between the tax basis of an asset or liability and its carrying amount on the balance sheet are used to calculate future income tax assets or liabilities. Future income tax assets or liabilities are calculated using tax rates anticipated to apply in the periods that the temporary differences are expected to reverse.

FLOW-THROUGH SHARES Resource expenditure deductions for income tax purposes related to exploration and development activities funded by flow-through share issues are renounced to investors in accordance with income tax legislation. The estimated tax benefits transferred to shareholders are recorded as a future income tax liability and a reduction in share capital, at the time the renunciation documents are filed with the appropriate tax authorities.

REVENUE RECOGNITION Revenue from the sale of oil and natural gas is recorded when title passes to an external party.

HEDGE ACCOUNTING Hedge accounting continues to be optional, however, there are standards for when and how hedge accounting may be applied. At inception of the hedge, the Company must formally document the designation of the hedge, the risk management objectives, the hedging relationships between the hedged items and the hedging items and the methods for testing the effectiveness of the hedge. The Company assesses, both at inception of the hedge and on an on-going basis, whether the derivatives designated as hedges are highly effective in off-setting changes in fair values or cash flows of hedged items.

The Company has not applied hedge accounting with respect to the financial derivative contracts referred to in these financial statements.

STOCK-BASED COMPENSATION The Company has a stock based compensation plan and uses the fair-value method to record compensation expense with respect to stock options granted. The fair value of each option granted is estimated on the date of grant and a provision for the costs is provided for as contributed surplus over the vesting period outlined in the option agreement. The consideration received by the Company on the exercise of share options is recorded as an increase to share capital together with

For the years ended December 31, 2007 and December 31, 2006
[ALL TABULAR AMOUNTS IN 000s, UNLESS OTHERWISE STATED]

corresponding amounts previously recognized in contributed surplus. Forfeitures are accounted for as they occur which could result in recoveries of the compensation expense.

COMPREHENSIVE INCOME Comprehensive income is defined as the change in equity from transactions and other events from non-owner sources and other comprehensive income comprises revenues, expenses, gains and losses that, in accordance with GAAP, are recognized in comprehensive income but excluded from net earnings.

PER SHARE AMOUNTS Basic per share amounts are calculated using the weighted average number of shares outstanding during the year. Weighted average number of shares is determined by relating the portion of time within the reporting period that common shares have been outstanding to the total time in that period.

Diluted per share amounts are calculated using the treasury stock method which assumes that any proceeds obtained on exercise of share options or other dilutive instruments would be used to purchase common shares at the average market price during the period. The weighted average number of shares outstanding is then adjusted by the net change.

CHANGES IN ACCOUNTING POLICIES AND PRACTICES Effective January 1, 2007, the Company has adopted the following new Canadian Institute of Chartered Accountants ("CICA") Handbook sections:

(i) Section 1530, Comprehensive Income;
(ii) Section 3251, Equity;
(iii) Section 3855, Financial Instruments – Recognition and Measurement;
(iv) Section 3865, Hedges; and
(v) Section 1506, Accounting Changes.

The standards have been adopted prospectively and therefore, the comparative interim financial statements have not been restated. The adoption of these Handbook sections has no impact on opening retained earnings or opening accumulated other comprehensive income.

Under the revised standards, voluntary changes in accounting polices are permitted only if they result in financial statements which provide more reliable and relevant information. Accounting policy changes are applied retrospectively unless it is impractical to determine the period or cumulative impact of the change. Corrections of prior period errors are applied retrospectively and changes in accounting estimates are applied prospectively by including these changes in earnings These standards are effective for all changes in accounting policies, changes in accounting estimates and corrections of prior period errors initiated in periods beginning on or after January 1, 2007.

FUTURE CHANGES IN ACCOUNTING POLICIES The following is an overview of CICA accounting standard changes that the Company will be required to adopt in future years:

(i) Section 1535, Capital Disclosures;
(ii) Section 3862, Financial Instruments – Disclosures; and
(iii) Section 3863, Financial Instruments – Presentation.

Section 1535 establishes disclosure requirements about an entity's capital and how it is managed. The purpose will be to enable users of the financial statements to evaluate the entity's objectives, policies and processes for managing capital.

Sections 3862 and 3863 will replace section 3861, Financial Instruments – Disclosure and Presentation, revising and enhancing its disclosure requirements, and carrying forward unchanged its presentation requirements. These new sections will place increased emphasis on disclosures about the nature and extent of risks arising from financial instruments and how the entity manages those risks

These new standards will be effective for fiscal years beginning on or after October 1, 2007 and the Company will adopt them on January 1, 2008.

For the years ended December 31, 2007 and December 31, 2006
[ALL TABULAR AMOUNTS IN 000s, UNLESS OTHERWISE STATED]

[NOTE 2] PROPERTY, PLANT AND EQUIPMENT

At December 31, 2007	Cost	Accumulated depletion, depreciation and amortization	Net book value
Oil and gas properties, plant and equipment	$ 620,274	$ 165,194	$ 455,080
Head office assets	1,165	499	666
	$ 621,439	$ 165,693	$ 455,746
[illegible]			
Oil and gas properties, plant and equipment	$ 439,264	$ 102,173	$ 337,091
Head office assets	852	344	508
	$ 440,116	$ 102,517	$ 337,599

At December 31, 2007, oil and gas properties with a cost of $34.9 million (December 31, 2006 - $32.8 million) relating to unproved properties have been excluded from the depletion and depreciation calculation. Future capital costs required to develop proved reserves in the amount of $37.8 million (2006 - $30.9 million) are included in the depletion and depreciation calculation.

During the twelve months ended December 31, 2007, the Company capitalized $0.5 million (2006 – $0.5 million) with respect to employee salaries directly relating to exploration and development activities.

As a result of ceiling test calculations at December 31, 2007 and December 31, 2006, the Company was not required to record an impairment loss.

The forecasted future prices used for the next five years in the ceiling test evaluation of the Company's proved reserves as at December 31, 2007 were as follows:

	2008	2009	2010	2011	2012
Oil [$/BBL]	$ 80.70	$ 77.24	$ 75.32	$ 73.46	$ 72.89
NGLs [$/BBL]	72.23	69.03	67.77	65.99	65.48
Natural gas [$/MCF]	6.93	7.70	8.22	8.24	8.15

Prices escalate at approximately 1.7% thereafter

For comparative purposes the forecasted future prices used for the next five years in the ceiling test evaluation of the Company's proved reserves as at December 31, 2006 were as follows:

	2007	2008	2009	2010	2011
Oil [$/BBL]	$ 67.87	$ 71.48	$ 63.89	$ 59.17	$ 55.51
NGLs [$/BBL]	60.00	62.56	55.95	51.72	48.54
Natural gas [$/MCF]	8.26	9.23	8.31	8.10	8.28

Prices escalate at approximately 1.5% thereafter

For the years ended December 31, 2007 and December 31, 2006
[ALL TABULAR AMOUNTS IN 000s, UNLESS OTHERWISE STATED]

[NOTE 3] BANK DEBT

	December 31, 2007	December 31, 2006
Bank loan	$ 19,900	$ 51,800
Bankers' acceptances	100,000	50,000
	$ 119,900	$ 101,800

Celtic has a committed term credit facility with Canadian financial institutions. The authorized borrowing amount under this facility is $165.0 million. Interest is payable monthly for borrowings through direct advances. Interest rates fluctuate based on a pricing grid and range from bank prime to bank prime plus 1.50%, depending upon the Company's then current debt to cash flow ratio of between less than one and a half times to greater than three times. At December 31, 2007, interest was payable at bank prime plus 0.25%. Under the credit facility, borrowings through the use of bankers' acceptances are also available. The Company has a fixed rate bankers' acceptance in the amount of $100.0 million maturing on April 21, 2008 at an aggregate interest rate of 5.4%. Security is provided for by a floating charge debenture over all assets in the amount of $250.0 million, general assignment of book debts and a fixed charge on the Company's major producing petroleum and natural gas properties.

Repayments of principal are not required provided that the borrowings under the facility do not exceed the authorized borrowing amount and the Company is in compliance with all covenants, representations and warranties. The maturity date for the credit facility is May 3, 2008, at which time the banks will complete their annual review. The banks may conduct an interim review prior to May 3, 2008.

[NOTE 4] ASSET RETIREMENT OBLIGATION

The following table provides a reconciliation of the carrying amount of the obligation associated with the retirement of oil and gas properties:

	December 31, 2007	December 31, 2006
Asset retirement obligation, beginning of period	$ 4,885	$ 4,294
Liabilities incurred, net of liabilities disposed	864	736
Liabilities settled	(1,021)	(646)
Revisions to estimated liabilities	671	(25)
Accretion expense	320	526
Asset retirement obligation, end of period	$ 5,719	$ 4,885

The key assumptions, on which the carrying amount of the asset retirement obligations is based, include a credit-adjusted risk-free rate of 8.5% and an inflation rate of 3.0%. The total undiscounted amount of the estimated cash flows required to settle the obligations is $23.9 million (December 31, 2006 - $20.7 million). The inflated value of estimated cash flows required to settle the obligations at a future period at the time the asset is retired is $63.8 million (December 31, 2006 - $43.6 million). The expected timing of payment of the cash flows required to settle the obligations ranges from 2 years to 51 years.

For the years ended December 31, 2007 and December 31, 2006
[ALL TABULAR AMOUNTS IN 000s, UNLESS OTHERWISE STATED]

[NOTE 5] SHARE CAPITAL

(A) AUTHORIZED

Unlimited number of common shares.
Unlimited number of preferred shares.

(B) ISSUED The following table summarizes the changes in common shares outstanding for the years ended December 31, 2006 and December 31, 2007:

	Common Shares		Amount
Balance, December 31, 2005	28,973	$	89,812
Issued for cash on exercise of stock options	207		1,035
Amount relating to exercised options previously recorded as contributed surplus	-		200
Issued for cash through private placement	2,000		26,300
Issued for cash through flow-through private placement	1,000		17,250
Future income tax benefit transferred on flow-through share issue	-		(5,367)
Share issue costs, after future income taxes	-		(1,389)
Balance, December 31, 2006	32,180	$	127,841
Issued for cash on exercise of stock options	786		3,411
Amount relating to exercised options previously recorded as contributed surplus	-		556
Issued for cash through private placement	3,200		45,920
Issued for cash through flow-through private placement	1,500		24,975
Share issue costs, after future income taxes	-		(2,523)
Balance, December 31, 2007	37,666	$	200,180

(C) FLOW-THROUGH SHARES On February 27, 2007, Celtic issued 1.5 million common shares on a flow-through basis at an issue price of $16.65 per share for gross proceeds of $25.0 million. At December 31, 2007, the Company had an estimated $12.5 million remaining obligation to incur Canadian Exploration Expenditures ("CEE"), which must be completed by December 31, 2008.

(D) STOCK OPTIONS Celtic has a stock option plan that provides for granting of stock options to directors, officers, employees and consultants. Stock options granted under the stock option plan have a maximum term of five years to expiry. Vesting is determined by the Company's board of directors. However, the majority of the options granted vest equally over a three year period commencing on the first anniversary date of the grant. The exercise price of each stock option granted is determined as the closing market price of the common shares on the Toronto Stock Exchange on the day of grant. Each stock option granted permits the holder to purchase one common share of the Company at the stated exercise price.

NOTES TO THE FINANCIAL STATEMENTS

For the years ended December 31, 2007 and December 31, 2006
[ALL TABULAR AMOUNTS IN 000s, UNLESS OTHERWISE STATED]

The following table summarizes the changes in stock options outstanding during the years ended December 31, 2006 and December 31, 2007:

	Number of Options	Average Exercise Price
Balance, December 31, 2005	2,256	$ 6.58
Granted	581	12.53
Exercised	(207)	4.99
Forfeited	-	-
Balance, December 31 2006	2,630	$ 8.02
Granted	1,050	12.76
Exercised	(786)	4.34
Forfeited	(68)	12.94
Balance, December 31, 2007	2,826	$ 10.69

The Company uses the fair-value method to record stock based compensation expense with respect to stock options granted. The fair value of each option granted is estimated on the date of grant using the Black-Scholes option pricing model with weighted average assumptions for grants as follows:

Twelve months ended December 31,	2007	2006
Risk free interest rate [%]	4.50	4 25
Expected life [YEARS]	3.0	3.0
Expected volatility [%]	20	20
Expected dividend yield	-	-
Fair value of options granted during the year [$/SHARE]	2.54	2 49

The following table summarizes information regarding stock options outstanding at December 31, 2007:

Range of exercise prices per share	Number of options outstanding	Weighted average remaining term in years	Weighted average exercise price per share for options outstanding	Number of options exercisable	Weighted average exercise price per share for options exercisable
$ 4.01 to $ 6.00	468	0.8	$ 5.63	468	$ 5.63
$ 6.01 to $ 8.00	303	1.6	7.67	303	7.67
$ 8.01 to $ 10.00	28	1.8	8.65	28	8.65
$ 10.01 to $ 12.00	466	2.6	11.22	311	11.22
$ 12.01 to $ 14.00	1,511	4.1	12.60	180	12.51
$ 14.01 to $ 16.00	50	4.4	14.70	-	-
Total	2,826	3.0	$ 10.69	1,290	$ 8 48

For the years ended December 31, 2007 and December 31, 2006
[ALL TABULAR AMOUNTS IN 000s, UNLESS OTHERWISE STATED]

[NOTE 6] INCOME TAXES

(A) FUTURE INCOME TAX EXPENSE The provision for income taxes differs from the expected amount calculated by applying the combined Federal and Provincial corporate income tax rate as a result of the following:

	2007	2006
Earnings before taxes	$ 5,679	$ 47,096
Statutory combined federal & provincial income tax rate [%]	32.12	34.49
Expected income taxes	$ 1,824	$ 16,244
Increase (decrease) resulting from:		
Non-deductible Crown payments	-	2,078
Non-deductible stock-based compensation costs	467	387
Non-taxable Provincial royalty credits [ARTC]	-	(60)
Allowable resource allowance deduction	-	(2,797)
Benefit relating to changes in future income tax rates	(4,842)	(4,008)
Other adjustments	32	21
Provision for (recovery of) future income taxes	$ (2,519)	$ 11,865

(B) FUTURE INCOME TAX LIABILITY The components of future income taxes are as follows:

At December 31	2007	2006
Future income tax liabilities		
Property, plant and equipment	$ 39,545	$ 38,642
Unrealized financial derivative gains	273	4,202
Future income tax assets:		
Asset retirement obligation costs	(1,596)	(1,505)
Share issue costs	(1,314)	(936)
Other income tax assets	(39)	(39)
Net future income tax liability	$ 36,869	$ 40,364
Less: current portion	(273)	(4,202)
Future income taxes	$ 36,596	$ 36,162

[NOTE 7] EARNINGS PER SHARE

The Company uses the treasury stock method to determine the dilutive effect of stock options and other dilutive instruments. Under this method, only "in-the-money" dilutive instruments impact the calculations in computing diluted earnings per share.

NOTES TO THE FINANCIAL STATEMENTS

For the years ended December 31, 2007 and December 31, 2006
[ALL TABULAR AMOUNTS IN 000s, UNLESS OTHERWISE STATED]

In computing diluted earnings per share, 0.3 million (2006 – 0.8 million) shares were added to the 35.5 million (2006 – 30.6 million) weighted average number of common shares outstanding during the twelve month period for the dilutive effect of stock options.

[NOTE 8] COMMITMENTS

The Company is committed to future payments under the following agreements:

	2008	2009	2010	2011	Total
Operating lease – office building	$ 568	$ 568	$ 568	$ 189	$ 1,893
Operating lease – vehicles	137	57	-	-	194
Firm transportation agreements	252	92	-	-	344
Exploration and development	12,481	-	-	-	12,481
	$ 13,438	$ 717	$ 568	$ 189	$ 14,912

Rental leases relating to office space expire on April 30, 2011. Exploration and development commitments relate to the Company's obligation pursuant to a flow-through share issue (see Note 5(c)).

[NOTE 9] FINANCIAL INSTRUMENTS

(A) FAIR VALUES OF FINANCIAL ASSETS AND LIABILITIES Financial instruments of the Company consist mainly of receivables, payables, bank debt and financial derivative contracts, all of which are included in these financial statements. At December 31, 2007, the classification of financial instruments and the carrying amounts reported on the balance sheet and their estimated fair values are as follows:

Classification	Carrying Amount	Fair Value
Loans and receivables [accounts receivable]	$ 25,751	$ 25,751
Held-to-maturity investments	-	-
Held-for-trading instruments [financial derivative contracts]	925	925
Available-for-sale financial assets	-	
Other financial liabilities [accounts payable and bank debt]	(166,380)	(166,380)
Total	$ (139,704)	$ (139,704)

(B) CREDIT RISK The majority of the Company's accounts receivable is in respect of oil and gas operations. Celtic generally extends unsecured credit to these third parties, and therefore, the collection of accounts receivable may be affected by changes in economic or other conditions and may accordingly impact the Company's overall credit risk. Celtic has not experienced any material credit loss in the collection of receivables in 2007.

(C) INTEREST RATE RISK The Company is exposed to fluctuations in interest rates on its bank debt. Interest rate risk is mitigated through short-term fixed rate borrowings using bankers' acceptances.

For the years ended December 31, 2007 and December 31, 2006
[ALL TABULAR AMOUNTS IN 000s, UNLESS OTHERWISE STATED]

(D) FOREIGN EXCHANGE RATE RISK The Company is exposed to the risk of changes in the Canadian/U.S. dollar exchange rate on sales of commodities that are denominated in U.S. dollars or directly influenced by U.S. dollar benchmark prices.

(E) COMMODITY PRICE RISK MANAGEMENT The following is a summary of oil sales price derivative contracts in effect as at December 31, 2007, that has fixed future sales prices (fixed oil prices are based on the West Texas Intermediate (WTI) Index):

Daily quantity	Remaining term of contract	Fixed price per barrel [BBL]	
500 bbls/d	January 1 to December 31, 2008	$	89.00
500 bbls/d	January 1 to December 31, 2008	$	88.00
300 bbls/d	January 1 to December 31, 2008	US$	92.50
500 bbls/d	January 1 to December 31, 2008	US$	70.00

The fair value of the above oil contracts, mark-to-market at December 31, 2007 is an unrealized loss of $5.7 million.

The following is a summary of natural gas sales price derivative contracts in effect as at December 31, 2007, that has fixed future sales prices (fixed natural gas prices are based on the New York Mercantile Exchange ("NYMEX") Index):

Daily quantity	Remaining term of contract	Fixed price per mmbtu (NYMEX)
6,500 mmbtu/d (costless collar)	January 1 to December 31, 2008	US$8.00 (floor) US$9.05 (cap)

The following is a summary of natural gas sales price derivative contracts in effect as at December 31, 2007, that has fixed future sales prices (fixed natural gas prices are based on the AECO-C Index):

Daily quantity	Remaining term of contract	Fixed price per GJ(AECO)	
5,000 GJ/d	January 1 to October 31, 2008	$	7.43
20,000 GJ/d	January 1 to October 31, 2008	$	7.02

The fair value of the above natural gas contracts, mark-to-market at December 31, 2007 is an unrealized gain of $6.6 million.

For the years ended December 31, 2007 and December 31, 2006
[ALL TABULAR AMOUNTS IN 000s, UNLESS OTHERWISE STATED]

[NOTE 10] SUPPLEMENTAL CASH FLOW INFORMATION

Changes in non-cash working capital, excluding bank debt:

Twelve months ended December 31,	2007	2006
Accounts receivable	$ (6,473)	$ 3,304
Prepaid expenses	186	(545)
Accounts payable and accruals	19,676	(19,603)
Change in non-cash working capital	$ 13,389	$ (16,844)
Relating to:		
Operating activities	$ 2,772	$ 3,739
Investing activities	10,617	(20,583)
Change in non-cash working capital	$ 13,389	$ (16,844)

During the reporting period, the Company made the following cash outlays in respect of interest expense and capital taxes:

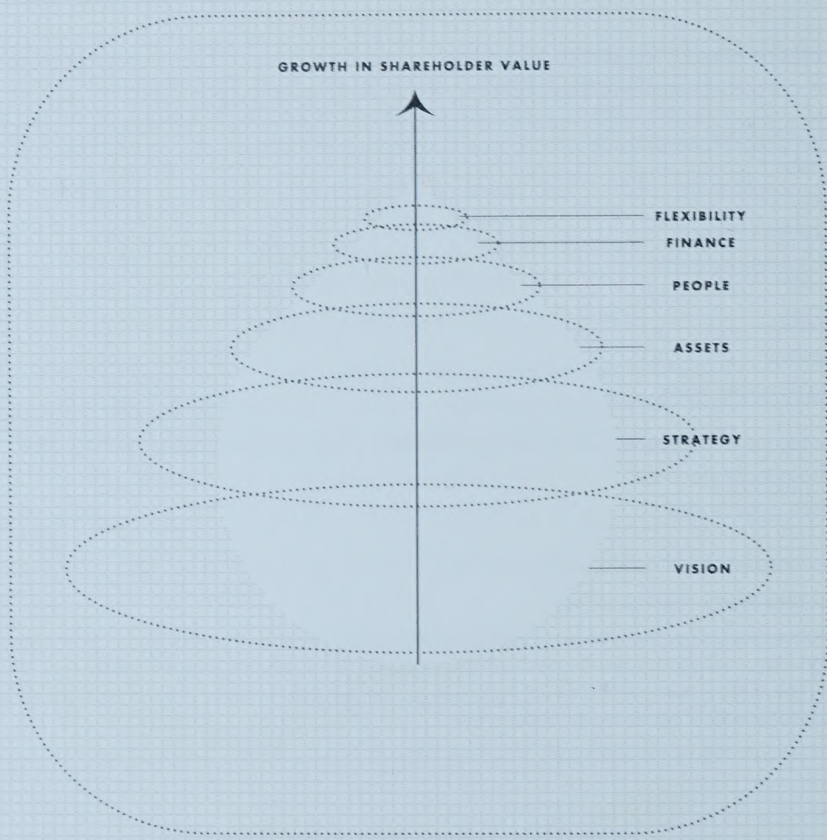
Twelve months ended December 31,	2007	2006
Interest	$ 6,533	$ 4,310
Capital tax	-	195

[NOTE 11] RELATED-PARTY TRANSACTIONS

The Company has retained the law firm of Borden Ladner Gervais LLP ("BLG") to provide Celtic with legal services. William C. Guinan, a director, chairman and corporate secretary of Celtic is a partner of this law firm. During the year ended December 31, 2007, the Company paid a total of $0.3 million (2006 $0.2 million) to BLG for legal fees and disbursements (including GST). The Company expects to continue using the services of this law firm from time to time.

It's tough to predict the future in this industry. And while we have consistently delivered results for shareholders since 2002, we can't just sit back with our fingers crossed. We have to continue to create our own success through the fundamentals of finance, people, assets and strategy. I guess you could say those are the leaves of our clover. And with our vision for a better future, and flexibility in capturing new opportunities, one thing is clear. **Clover or no clover, our success has nothing to do with luck.**

FOCUS ON THE FUTURE



The Company's solid financial platform is the foundation for all we do at Celtic Exploration. We employ people with the experience and expertise to deploy our capital investments where they can earn the greatest long-term return for our shareholders.

We choose assets with an eye to the future, favoring those that offer profitable production today and dramatic upside for tomorrow. Our dual-pronged strategy combines aggressive exploration with strategic acquisitions. Our long-term vision and operational flexibility will continue to deliver exceptional growth.

CORPORATE INFORMATION

BOARD OF DIRECTORS

ROBERT J. DALES [2, 3, 4]
President, Valhalla Ventures Inc.

WILLIAM C. GUINAN [1, 5]
Partner, Borden Ladner Gervais LLP

ELDON A. MCINTYRE [2, 3, 4]
President, Jarrod Oils Ltd.

NEIL G. SINCLAIR [2, 4, 5]
President, Sinson Investments Ltd.

DAVID J. WILSON [3, 5]
President & Chief Executive Officer, Celtic Exploration Ltd.

OFFICERS

DAVID J. WILSON
President & Chief Executive Officer

SADIQ H. LALANI
Vice President, Finance & Chief Financial Officer

MICHAEL R. SHEA
Vice President, Land

DAVID C. MORGENSTERN
Vice President, Exploration

ALAN G. FRANKS
Vice President, Operations

1 Chairman of the Board
2 Member of the Audit Committee
3 Member of the Reserves Committee
4 Member of the Compensation Committee
5 Member of the Disclosure Committee

HEAD OFFICE

Suite 500, 505 Third Street S.W.
Calgary, Alberta T2P 3E6

Phone: 403.201.9153
Fax: 403.201.9163

www.celticex.com

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REGISTRAR AND TRANSFER AGENT

VALIANT TRUST COMPANY
Suite 310, 606 Fourth Street S.W.
Calgary, Alberta T2P 1T1

LEGAL COUNSEL

BORDEN LADNER GERVAIS LLP
Suite 1000, 400 Third Avenue S.W.
Calgary, Alberta T2P 4H2

BANKERS

NATIONAL BANK OF CANADA
Suite 2700, 530 Eighth Avenue S.W.
Calgary, Alberta T2P 3S8

AUDITORS

PRICEWATERHOUSECOOPERS LLP
Suite 3100, 111 Fifth Avenue S.W.
Calgary, Alberta T2P 5L3

EVALUATION ENGINEERS

SPROULE ASSOCIATES LIMITED
Suite 900, 140 Fourth Avenue S.W.
Calgary, Alberta T2P 3N3

STOCK EXCHANGE LISTING

Toronto Stock Exchange
Trading symbol "CLT"

CELTIC'S ANNUAL AND SPECIAL MEETING OF SHAREHOLDERS

Celtic's Annual Meeting of shareholders is scheduled for Wednesday, April 30, 2008 at 3:00 p.m., to be held at The Metropolitan Centre, 333 Fourth Avenue S.W., Calgary, Alberta.

ABBREVIATIONS

BBLS	barrels
MBBLS	thousand barrels
BBLS/D	barrels per day
BOE	barrels of oil equivalent
MBOE	thousand barrels of oil equivalent
BOE/D	barrels of oil equivalent per day
MCF	thousand cubic feet
MMCF	million cubic feet
BCF	billion cubic feet
MMCF/D	million cubic feet per day
MMBTU	million British Thermal Units
GJ	gigajoules
AECO-C	Alberta Energy Company "C" Meter Station of the Nova Pipeline System
API	American Petroleum Institute
ARTC	Alberta Royalty Tax Credit
CICA	Canadian Institute of Chartered Accountants
BIT	before income taxes
WTI	West Texas Intermediate

CONVERSION OF UNITS

Imperial = Metric
1 acre = 0.4 hectares
2.5 acres = 1 hectare
1 bbl = 0.159 cubic metres
6.29 bbls = 1 cubic metre
1 foot = 0.3048 metres
3.281 feet =1 metre
1 mcf = 28.2 cubic metres
0.035 mcf = 1 cubic metre
1 mile = 1.61 kilometres
0.62 miles = 1 kilometre
1 mmbtu = 1.054 GJ
0.949 mmbtu =1 GJ

Natural gas is equated to oil on the basis of 6 mcf = 1 BOE.

Celtic
EXPLORATION LTD.

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SUITE 500, 505 THIRD STREET S.W.
CALGARY, ALBERTA T2P 3E6